

Driehaus US Small Cap Equity Fund

Q2 2024 Commentary

Portfolio Management



**Jeff
James**



**Michael
Buck**



**Prakash
Vijayan**

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 18.0 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 US Small Cap 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 meaning Driehaus exercises discretionary investment authority over the Fund. The Fund was launched on 31st July 2019 and had AUM of USD 784m as of 30th June 2024. During the second quarter of 2024, the Fund outperformed its benchmark, the Russell 2000 Growth Index TR USD (the "Index"), returning 0.0% (I USD share class) compared to -2.9% for the Index.

Market Overview

The U.S. equity market experienced a mixed second quarter. Large caps experienced positive gains driven (again) by strength in the mega cap tech stocks. Large cap stocks outperformed small caps and mid caps overall, which were down in the low single digit percentage range for the quarter. Absent those select mega cap stocks, large caps would have performed similarly to small caps and the average U.S. stock.

The U.S. economy is moderating based on a slew of weaker data recently. Inflation data is also moderating and there are positive signs it is trending favorably towards the Federal Reserve's two percent target. Inflation is not at two percent yet, but most components of inflation suggest its trajectory is positive enough for the Fed to consider interest rate cuts in the second half of the year. For now, we view the slower economic growth as benign and not recessionary though the pace of economic data will be important to monitor near-term. Importantly, the slowing economic conditions appear to be having a favorable impact on inflation.

The broader market and the small cap indices, despite finishing down for the quarter, consolidated in a constructive manner. While many individual stocks and several industries outperformed as their earnings stood out, the market's consolidation was likely a function of market participants focusing on how economic and inflation data will frame the macro-outlook for the second half of the year and how it will influence the Fed's monetary policy.

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

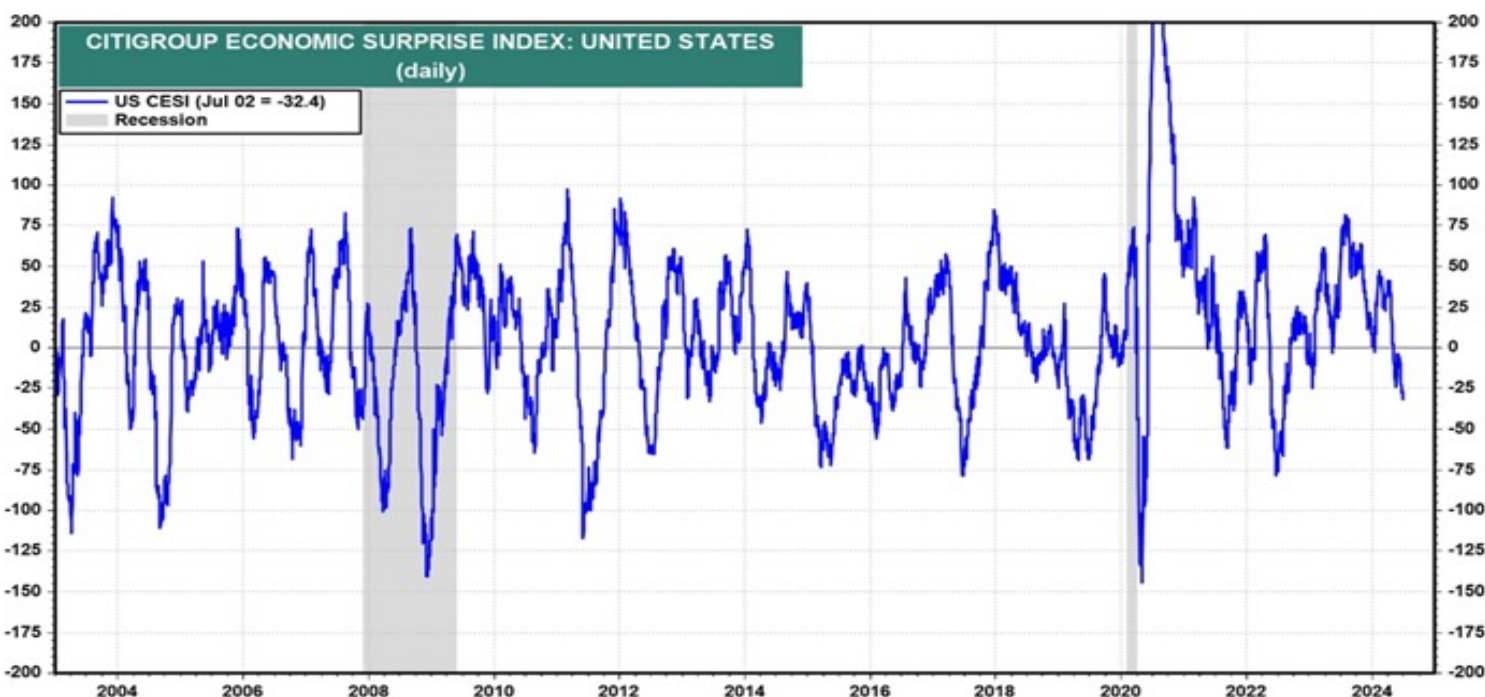
The most recent inflation data was encouraging as May and June's consumer price index (CPI) and producer price index (PPI) inflation readings were lower than expected. This along with rising unemployment claims raised market expectations that the Fed will ease monetary policy sooner rather than later. The first half of the year did see rate cut expectations pushed out to the right several times, but the market continues to expect two interest rate cuts this year with close to ninety percent odds of the first rate cut occurring in September. The reasons behind the rate cuts will be particularly important. Lower rates due to inflation approaching the Fed's target with positive economic conditions will be well received by the equity market. On the other hand, rate cuts due to the economy becoming too weak will likely not be well received.

Economic conditions

Economic conditions in the U.S. have slowed. Some of the economic data is becoming concerning but in aggregate terms economic growth remains positive. There could be several reasons for the slowdown. It is possible that the still inverted curve could be having its traditional detrimental impact, just on an exceptionally long lag. It is also possible that the sustained higher level of interest rates and the cumulative amount of inflation are negatively impacting economic demand, especially for the bottom half of consumers. On the other hand, it is also possible that the current slowdown is a mid-cycle slowdown that the economy has experienced many times in past cycles. Let's consider the strengths and weaknesses of the following important economic indicators:

- The Citi Economic Surprise Index dropped to its lowest level since August of 2022. However, as the chart below illustrates, it has reached this level many times during prior mid-cycle soft patches, and it is still well above the level reached during past recessions.

Exhibit 1: Citi Economic Surprise Index

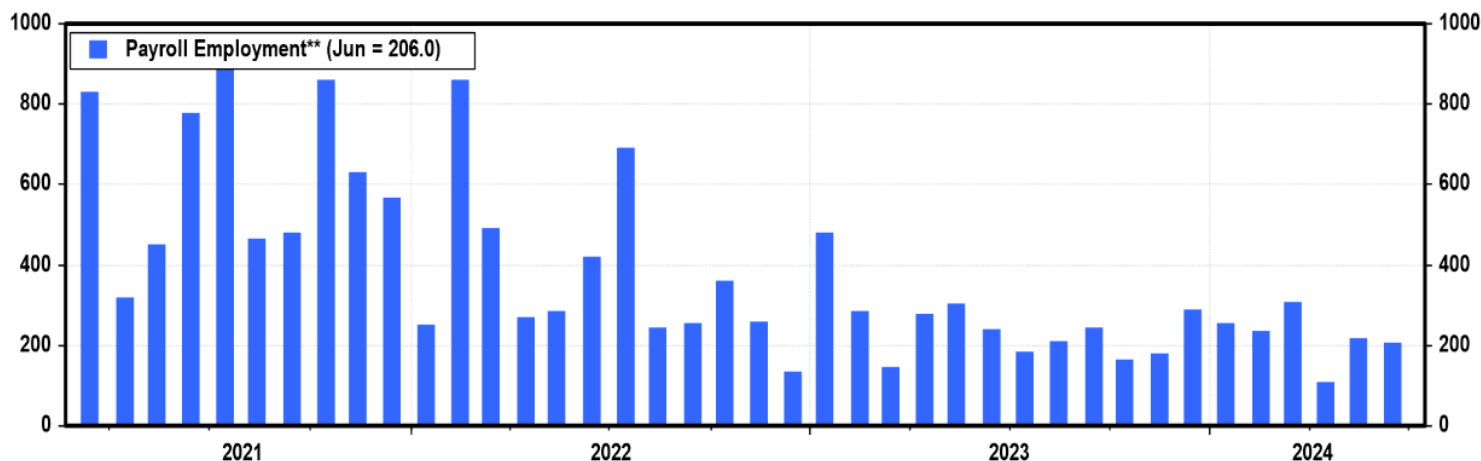


Source: Yardeni Research

- The labor market has slowed, and it is likely the key area of the economy that the market and the Fed are evaluating to gauge the status of both the economy and inflation. Here are some important labor market indicators:
 - Job gains did grow 206,000 in the month of June but have slowed to an average of 177,300 during the second quarter, down from 267,300 in the first quarter. Constructively, the second quarter average was within the range of average monthly job gains seen in 2018 (190,300) and 2019 (165,700). Overall, the trend of monthly jobs added is still solid; here is the monthly trend since early 2021:

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

Exhibit 2: Monthly Jobs

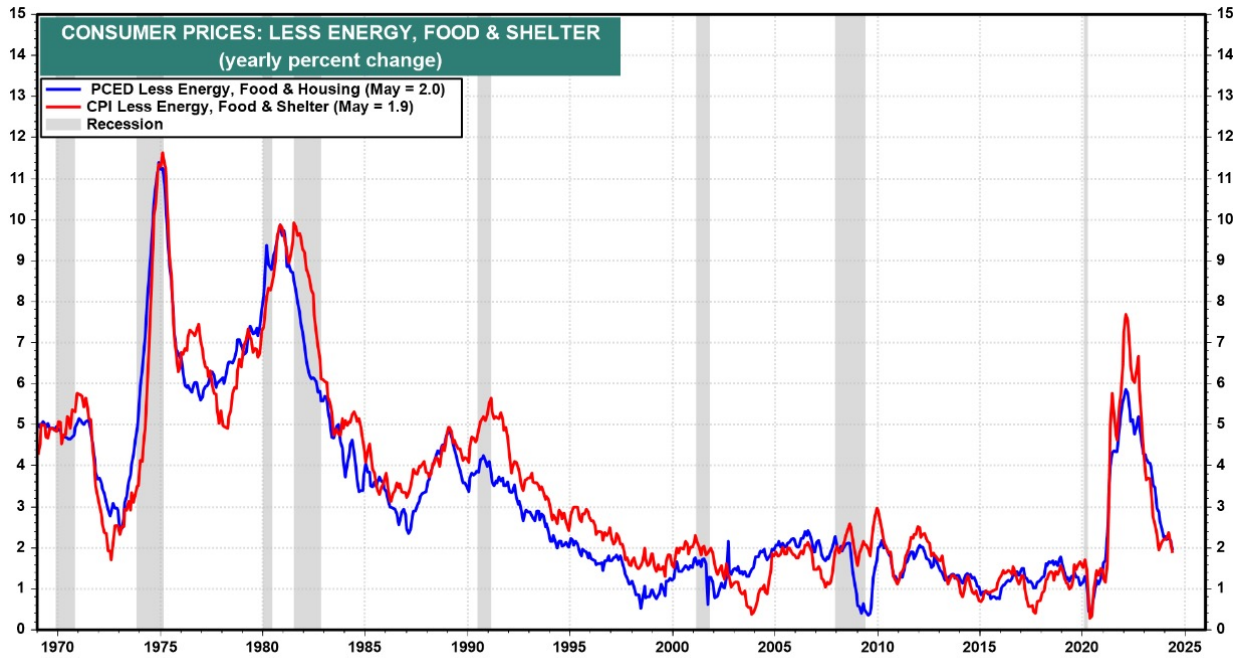


Source: Yardeni Research

- Job openings have also slowed from their pandemic highs but rose 221,000 in May to 8.14 million which is still a healthy level. Job openings per worker were flat at 1.2, well below the 2022 high but still well above historical levels since the year 2000.
- More concerning are jobless claims and continuing claims, both of which have risen in recent months. Also concerning is the unemployment rate which has risen to 4.1%, from its low of 3.4% in April of 2023 (a level not seen since the 1960s), and a rise of 0.5% within the past year which has triggered the Sahm Rule, which says historically a recession follows such an increase. There are some who argue that claims and unemployment were simply unusually low following the pandemic. Others suggest the adult unemployment rate is still low, considering that for age groups 25 years of age and above, the unemployment rate remains around 3%.
- Overall, this weakness in the data could be just a normalization, after an extended period of very tight labor conditions and since job gains and job openings remain favorable. Positively, modestly weaker current labor market conditions may encourage the Fed to ease. Either way the labor market needs to stabilize to give the market confidence that the trajectory of the general economy can remain positive.
- The Institute for Supply Management (ISM) data for both manufacturing and services has weakened below 50, indicating contraction, but remain above levels usually consistent with recessions.
- The Atlanta Fed's GDPNow, a running estimate of GDP growth based available economic data, also indicates a slowdown is underway. It is now projecting 1.5% GDP growth, down from 4.2% in the middle of the second quarter. This is a sizeable negative change, but it still suggests positive growth for the second quarter.

Inflation continues to trend favorably. Inflation readings in May were lower than expected. Most components of CPI and Personal Consumption Expenditures (PCE), the Fed's preferred measure of inflation, are trending lower. Shelter (primarily rents) remains the main component of inflation that is keeping the overall level of CPI and PCE elevated. It is reported on a lag and more real time measures of rent inflation suggest the rate of increase in rents has already returned to low levels. Core PCE and Core CPI, ex housing, reached 2.0% and 1.9%, respectively, in May, as displayed in the chart below. It also illustrates that this cycle of inflation was Covid related and has already returned to the Fed's target when adjusting for the lagging component of shelter.

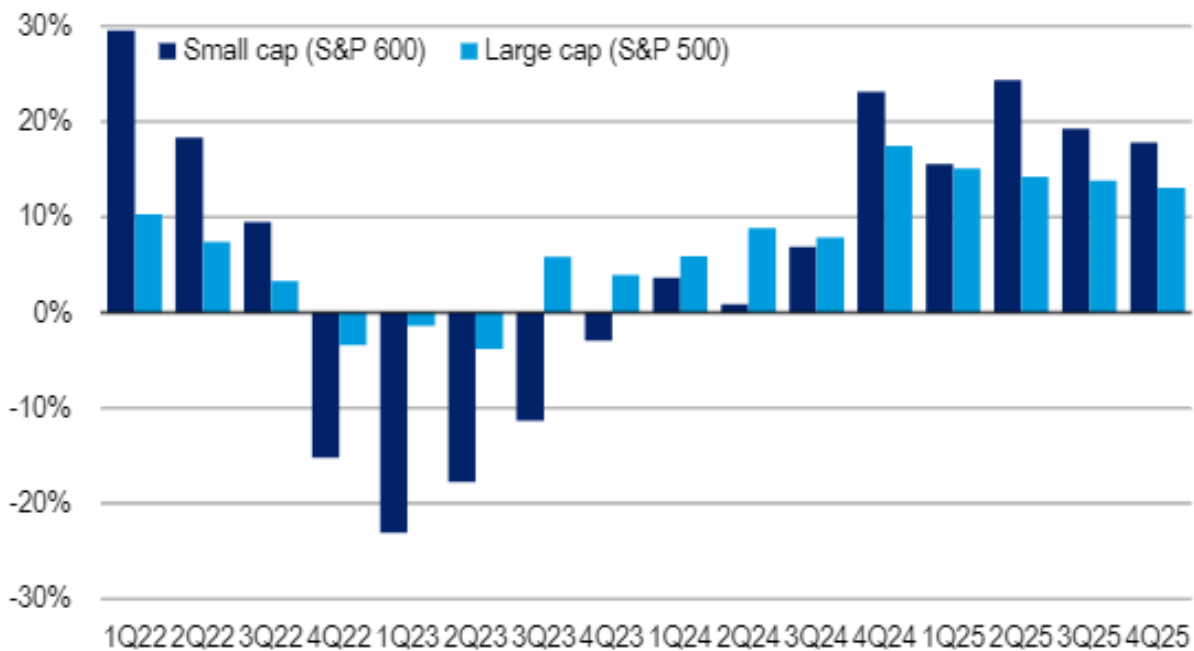
Exhibit 3: Core Consumer Prices ex Shelter Already at the Fed's 2% Target



Source: BEA, BLS and Yardeni Research

So, we have reached the halfway point of the year. Earnings overall are continuing to improve, for both small caps and large caps. As the bar chart below shows, after an earnings recession in 2023, aggregate earnings have turned positive on a year-over-year basis. While delayed a bit versus recent expectations, overall small cap earnings are still expected to outpace large cap earnings in the fourth quarter and in 2025. Many individual small cap companies are seeing earnings growing much faster than these averages.

Exhibit 4: Small cap profit growth expected to outpace large cap profits growth in Q4 and in 2025



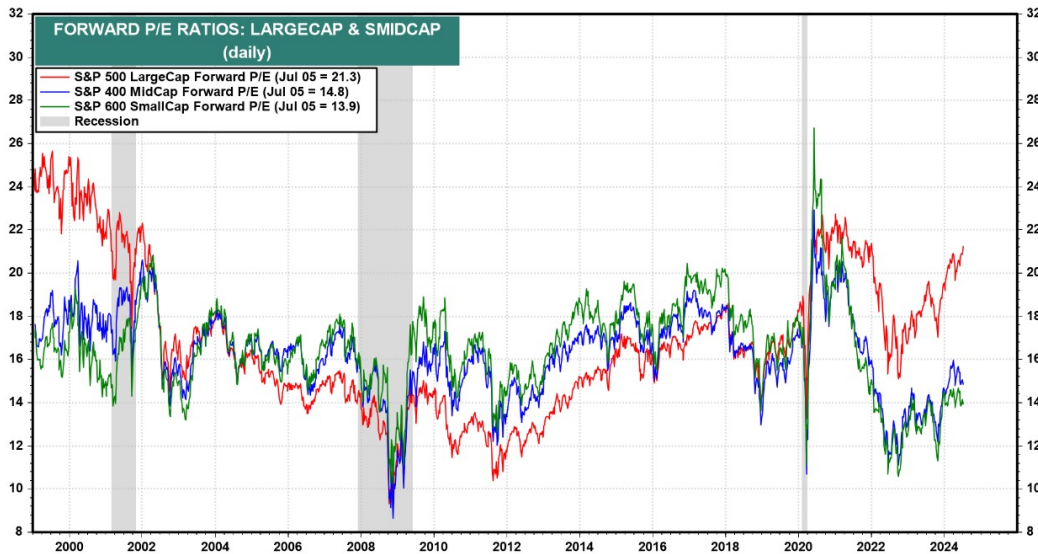
Source: BEA, BLS and Yardeni Research

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

I How are valuations?

Given the strength in large cap performance since the market highs in 2021, large cap valuations have traded at a premium to small cap valuations. Note the two valuation charts below. Whether looking at the Russell or the S&P indices, small caps currently trade at a deep relative discount. Historically, this is unusual as small caps have generally traded at a premium to large caps over the past several decades. This premium has likely been due to the inherently bigger growth potential and greater prospects for M&A (mergers and acquisitions). The first valuation chart below also shows how the absolute and relative valuations for small caps are both at a major discount compared to the past two and a half decades.

Exhibit 5: Small Caps remain historically cheap on an absolute and relative basis



Source: Yardeni Research

Exhibit 6: Small Caps remain historically cheap vs large caps

Relative Forward P/E: Russell 2000 vs Russell 1000, 1985-6/30/2024



Source: BofA Global Research

Overall, the macro environment has become more uncertain on the economic front but clearer in terms of inflation. Assuming our base case scenario holds, where the current economic moderation stabilizes, earnings recover as consensus estimates assume, disinflation continues and the Fed leans dovish, the outlook for equities for the second half of the year could be quite attractive.

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

Looking at historical market performance, a positive first half of the year usually leads to a positive second half of the year, especially during Presidential election years. Of course, if the recent economic weakness deteriorates further or if the improvement in inflation were to stall, the outlook for equities would become more bearish. As always, we will be monitoring these macro developments carefully as they will play a heavy role in the market's outlook, and they will influence our selection of individual stocks and their industries.

I Performance Review

For the June quarter, the Driehaus US Small Cap Equity Fund outperformed its benchmark by 290 basis points. The Fund gained 0.0% (I USD share class) net of fees, while the Russell 2000 Growth Index was down -2.9%, the Russell 2000 fell 3.6%, and the S&P 500 grew 4.3%.

Individual company earnings and their fundamental outlooks were strong for our holdings during the second quarter. These bottom-up results are supported by multiple themes and industry trends that we view as sustainable. In terms of attribution, the portfolio's outperformance was primarily driven by a strong stock selection effect of 3.5%, although this was slightly offset by a negative sector allocation effect of 28 basis points. The consumer discretionary sector led the way, contributing outperformance of 1.3%, the technology sector contributed outperformance of 1.1%, and the healthcare sector contributed outperformance of 1.0%.

For more detail by sector, the June quarter performance is summarised as follows (in order of relative outperformance):

Consumer Discretionary

Consumer discretionary contributed 80 basis points in absolute terms and outperformed by 130 basis points in relative terms, as our holdings gained 6.4% vs a loss of 5.7% for the benchmark's consumer discretionary holdings. We saw strength in restaurants, specialty retail, and an auto dealer. Four different restaurant holdings were particularly strong as they reported positive earnings surprises, strong same store sales, and continued robust unit growth. Homebuilding is a sub-industry that we reduced as the group began to lag and fundamentals slowed due to unfavorable home affordability. Overall, we did increase our sector exposure by 74 basis points, ending the quarter with a slight overweight exposure at 10.8%, versus 10.0% for the index.

Technology

Technology added 12 basis points in absolute performance and outperformed by 106 basis points versus the index, as our holdings returned 2.9% versus a loss of 3.3% for the index's holdings. All of the outperformance, 114 basis points, came from the semiconductor group, as our semi holdings appreciated 30.9% versus 10% for the index. A handful of holdings had strong earnings reports and are benefitting from the hardware infrastructure buildout to support AI (Artificial Intelligence) applications. These companies included semi cap equipment companies as well as semiconductor or component suppliers to data centers. During the quarter we did increase our exposure to semiconductors, raising our overweight from 0.6% to 3.8% as the fundamental outlook for our holdings and the industry as a whole have improved dramatically.

Software saw some outperformers during the quarter, but we continue to be underweight the group as IT budgets are shifting away from enterprise software towards AI and its supporting infrastructure. Cybersecurity remains a robust area within software as cyber-attacks continue to grow in number and sophistication. Several industries have been hard hit this year by cyber-attacks that have severely disrupted their operations in high profile attacks.

We increased our tech sector exposure by 125 basis points, moving from underweight to start the quarter to a small overweight by the end of the quarter. The increase in sector exposure was driven by a variety of hardware companies tied to AI, partially offset by a reduction in the software group as well as a large reduction in a top holding that grew far outside of our typical market cap range via appreciation.

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

Healthcare

Healthcare added 81 basis points in absolute returns and outperformed by 98 basis points as our holdings gained 3% versus a decline of 1.8% for the index. All of the outperformance came from the medical device sub-industry as it contributed 112 basis points in relative outperformance. Among the med device holdings that performed well, two were focused on ophthalmology and another on diabetes. But the key performer in the quarter was an innovative company servicing the organ transplant market. This holding gained 103% as it reported another large quarterly earnings surprise. Its revenues grew 133% year-over-year, and which was well above expectations, and it generated substantial operating leverage that produced earnings per share of 35 cents vs the consensus estimate of two cents. It also raised its forward guidance significantly.

Biotech took a break from its outperformance over the prior two quarters as the group was down very modestly (3% vs a decline of 2% for the index) and it detracted 19 basis points. We finished the quarter essentially inline, with a 12.9% weighting vs 13% for the index. Our absolute weighting did not change during the quarter. Within biotech we remain encouraged fundamentally as we believe our holdings have very promising and innovative clinical stage therapies demonstrating superior efficacy and safety in important disease indications, such as obesity, epilepsy, endocrinology, diabetes, neurology, autoimmune diseases, vaccines, and oncology. We anticipate promising results from upcoming clinical trials.

Most of our healthcare exposure continues to be in medical devices and biotech on a sub-industry basis. Our healthcare sector weighting increased 120 basis points during the quarter but our relative underweight expanded by the end of the quarter as the index increased its sector weight from 21.3% to 25.1% with the annual Russell rebalance occurring at the end of the quarter.

Industrials

Industrials detracted 26 basis points in absolute terms and contributed 71 basis points of relative outperformance as our holdings declined 0.8% though outperforming the 3.8% decline for the industrial sector in the index. We remain overweight the sector, but we did decrease the exposure by 230 basis points, to 23.7% vs 21.6% for the index. We continue to be positive on the sector as reshoring remains a strong theme. We also hold positions benefiting from attractive trends within commercial aerospace, infrastructure, and data centers where AI is driving demand for various technologies and equipment.

Energy

The energy sector detracted 13 basis points in absolute returns but contributed 6 basis points in relative returns. One uranium miner continued to perform well. Within oil and gas, performance was mixed as oil service companies performed well but E&Ps (Exploration and Production) pulled back in price after recent strength earlier in the year and as the underlying commodities were volatile. We reduced exposure to some of the oil levered E&Ps during the quarter. Our overweight position overall was reduced to 5.8% vs 4.2% for the index.

Consumer Staples

Consumer staples contributed 6 basis points in absolute terms but detracted 14 basis points in relative terms. While we reduced our exposure from over 7.1% to 6.2% during the quarter, this still equates to an overweight versus the index at 3.3%. Among our holdings a specialty grocery store and a pet food supplier outperformed as they continue to gain share and post strong earnings surprises. This strength was offset by weakness in an energy drink company. This holding has been a significant outperformer for the past several years for the portfolio, but the company experienced sharp revenue deceleration during the quarter as it faces tough comparisons of three consecutive years of one hundred percent plus revenue growth. We still like the stock long term but believe that the stock is going through a valuation adjustment as it seeks to stabilize its growth trend at a more modest level. As a result, we reduced the position significantly.

Financials

Financials detracted 63 basis points in absolute terms and 24 basis points in relative terms. All of the underperformance came from specialty insurance as a couple positions pulled back in price after positive performance last year and in the

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

first quarter. One position experienced a lackluster quarter versus elevated expectations and another position pulled back as fears of a very active hurricane season resulted in some multiple compression.

We remain positive on the insurance industry as it is undergoing significant positive change in pricing and the supply/demand environment. We are also positive on other holdings in the capital markets and regional banking sub-industries. We did reduce our exposure to the sector 7.2% to 5.6% and maintain an underweight versus 7.8% for the index.

I Outlook & Positioning

Equities performed in a mixed fashion during the June quarter as the mega cap stocks continued to outperform and investors monitor the macro environment as both economic data and inflation continue to moderate.

Our positive outlook consists of economic growth stabilizing (we believe it will stabilize despite the current soft patch), favorable inflation trends, a neutral to dovish Federal Reserve monetary policy position, the prospect of rate cuts later in the year and improving earnings. Small caps also continue to trade at a deep discount to large caps. The market's breadth and overall technical picture also remain attractive.

A more bearish outlook would include continued economic weakness or inflation that becomes sticky and doesn't trend lower, either of which will reduce equity multiples. Other key bearish variables could be weaker earnings, US political disfunction and major geopolitical issues outside of the U.S. We continue to lean positively, as we see the economy, inflation and earnings continuing to trend in a favorable direction.

In terms of portfolio positioning, we have an attractive mix of secular and cyclical growth holdings with strong earnings. By sector, industrials are our largest absolute weight, followed by healthcare, technology, and consumer discretionary. On a relative basis, the Fund is overweight industrials, consumer staples, energy, and technology. The Fund is underweight healthcare, financials and materials.

Sincerely,

Heptagon Capital and Driehaus Capital Management

Sector performance attribution- Q2 2024

GICS Sector	Driehaus Small Cap Growth Composite (Port) (%)		Russell 2000 Growth Index (Bench) (%)		Attribution Analysis (%)		
	Port Avg. Weight	Port Contrib To Return	Bench Avg. weight	Bench Contrib To Return	Allocation Effect	Selection + Interaction	Total Effect
Comm. Services	0.79	-0.06	1.96	0.05	-0.07	-0.08	-0.15
Consumer Discretionary	10.25	0.80	10.44	-0.58	0.00	1.31	1.31
Consumer Staples	6.56	0.06	4.50	0.28	0.17	-0.30	-0.14
Energy	8.56	-0.13	4.70	-0.11	0.00	0.07	0.07
Financials	6.30	-0.63	6.06	-0.33	-0.01	-0.22	-0.23
Health Care	21.21	0.81	21.31	-0.35	0.01	0.98	0.99
Industrials	24.61	-0.26	20.25	-0.74	-0.05	0.73	0.68
Information Technology	17.4	0.12	23.74	-0.89	-0.08	1.15	1.06
Materials	3.66	-0.16	4.25	-0.19	-0.15	0.03	-0.11
Real Estate	0.00	0.00	1.49	-0.12	0.07	0.00	0.07
Utilities	0.00	0.00	1.31	0.03	-0.06	0.00	-0.06
Cash	0.66	0.00	0.00	0.00	0.03	0.00	0.03
Other*	0.00	-0.14	0.00	0.00	-0.13	0.00	-0.13
Total	100.00	0.42	100.00	-2.96	-0.27	3.65	3.38

Sources: Driehaus Capital Management LLC, Factset Research Systems, Inc., eVestment Alliance

*Other refers to securities not recognised by Factset.

Data as of 30th June 2024

Annualized Total Returns as of 30th June 2024, gross of fees

	Q2 24	YTD	1-Year	3-Year	5-Year	10-Year
Driehaus Small Cap Growth Composite	0.5%	19.7%	25.7%	0.2%	14.9%	16.3%
Russell 2000 Growth Index TR	-2.9%	4.4%	9.1%	-4.9%	6.2%	7.4%

Source: Driehaus Capital Management, Morningstar

Driehaus manages the Irish regulated Driehaus US Small Cap Equity UCITS Fund according to the same investment principals, philosophy and execution of approach as it manages the Driehaus Small Cap Growth Composite, 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 Driehaus Small Cap Growth Composite is provided in the table above to show a longer track record for the underlying strategy.

The views expressed represent the opinions of Driehaus Capital Management, as 30th June 2024, are not intended as a forecast or guarantee of future results, and are subject to change without notice.

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

I Important Information

Past performance is not an indication or guarantee of future performance and no representation or warranty is made regarding future performance. This communication is for information purposes only. It is not an invitation or inducement to engage in investment activity.

The document is provided for information purposes only and does not constitute investment advice or any recommendation to buy or sell or otherwise transact in any investments.

The contents of this document are based upon sources of information which Heptagon Capital believes to be reliable. However, except to the extent required by applicable law or regulations, no guarantee, warranty or representation (express or implied) is given as to the accuracy or completeness of this document or its contents and, Heptagon Capital, its affiliate companies and its members, officers, employees, agents and advisors do not accept any liability or responsibility in respect of the information or any views expressed herein. 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. Where this document provides forward-looking statements which are based on relevant reports, current opinions, expectations and projections, actual results could differ materially from those anticipated in such statements. All opinions and estimates included in the document are subject to change without notice and Heptagon Capital is under no obligation to update or revise information contained in the document. Furthermore, Heptagon Capital disclaims any liability for any loss, damage, costs or expenses (including direct, indirect, special and consequential) howsoever arising which any person may suffer or incur as a result of viewing or utilising any information included in this document.

The document is protected by copyright. The use of any trademarks and logos displayed in the document without Heptagon Capital's prior written consent is strictly prohibited. Information in the document must not be published or redistributed without Heptagon Capital's prior written consent.

Heptagon Capital Limited has issued this communication as investment manager for Heptagon Fund ICAV, and is licensed to conduct investment services by the Malta Financial Services Authority. Heptagon Capital LLP, acting as Distributor, is authorised and regulated in the UK by the Financial Conduct Authority.

I 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.

I 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.

Authorised & Regulated by the Financial Conduct Authority (FRN: 403304)

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

I Disclaimers

FTSE Russell Source: London Stock Exchange Group ICAV and its group undertakings (collectively, the "LSE Group"). © LSE Group 2024. FTSE Russell is a trading name of certain of the LSE Group companies. Russell® is a trade mark of the relevant LSE Group companies and is/are used by any other LSE Group company under license. All rights in the FTSE Russell indexes or data vest in the relevant LSE Group company which owns the index or the data. Neither LSE Group nor its licensors accept any liability for any errors or omissions in the indexes or data and no party may rely on any indexes or data contained in this communication. No further distribution of data from the LSE Group is permitted without the relevant LSE Group company's express written consent. The LSE Group does not promote, sponsor or endorse the content of this communication.

The Global Industry Classification Standard ("GICS") was developed by and is the exclusive property and a service mark of MSCI Inc. ("MSCI") and S&P Global Market Intelligence ("S&P") and is licensed for use by Heptagon Fund ICAV. Neither MSCI, S&P, nor any other party involved in making or compiling the GICS or any GICS classifications makes any express or implied warranties or representations with respect to such standard or classification (or the results to be obtained by the use thereof), and all such parties hereby expressly disclaim all warranties of originality, accuracy, completeness, merchantability and fitness for a particular purpose with respect to any of such standard or classification. Without limiting any of the foregoing, in no event shall MSCI, S&P, any of their affiliates or any third party involved in making or compiling the GICS or any GICS classifications have any liability for any direct, indirect, special, punitive, consequential or any other damages (including lost profits) even if notified of the possibility of such damages.

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

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