

Tetragon Financial Group

Celebrating 10 years since its market debut

Tetragon Financial Group (TFG) achieved an 8.5% NAV total return in 2016, with positive contributions from all asset classes. Tender offers totalling US\$150m considerably enhanced returns, with shares repurchased at a substantial discount to NAV. While still wider than average among peers, Tetragon's share price discount to NAV narrowed by c 10 points over the year, reflecting its 32.7% share price total return. The 2016 dividend was raised by 3.9% to US\$0.6725, equating to a 5.3% yield. April 2017 marked Tetragon's 10th anniversary and its performance since launch compares favourably to peers, with an 11.3% pa NAV total return to end-April 2017.

12 months ending	Share price (%)	NAV (%)	MSCI AC World (%)	FTSE All-Share (%)	US 10y Govt Bond index (%)
30/04/13	45.0	17.3	15.7	12.9	5.3
30/04/14	(0.7)	16.1	15.0	19.9	(5.1)
30/04/15	1.0	8.2	8.0	(2.2)	8.3
30/04/16	7.9	12.8	(5.1)	(10.1)	4.2
30/04/17	35.2	8.1	15.8	6.1	(2.4)

Source: Thomson Datastream, Bloomberg, Edison Investment Research. Note: 12-month rolling discrete US dollar-adjusted total return performance up to last reported NAV.

Steady progress made in 2016 and Q117

All asset classes contributed positively during 2016, with notable contributions from US CLO investments, equity and credit hedge funds, and direct equity and credit investments. Investment income and gains net of expenses contributed c 7% to Tetragon's 8.5% NAV total return for the year, while tender offers totalling US\$150m contributed c 7%, outweighing a c 5% negative effect from factors which increased Tetragon's fully diluted share count over the year. TFG Asset Management's AUM grew by US\$2.4bn to US\$19.5bn during the year. NAV total return was 1.4% in Q117, with positive returns from all asset classes except equity and credit hedge funds, where one fund recorded a negative contribution after expenses. TFG Asset Management's AUM increased to US\$19.8bn during the quarter.

Outlook: Longer-term returns within target range

Tetragon sees investment returns at the lower end of its 10-15% ROE target range as consistent with the current low-Libor environment, and has not changed asset allocations. While CLO performance was negatively affected by tightening spreads in April 2017, Tetragon expects to benefit if loan spreads widen due to dampened new issuance following the implementation of risk retention rules. Tetragon is also optimistic over prospects for its hedge fund investments, notably European event-driven equities, with potentially compelling valuations seen among smaller-cap, non-index stocks and the potential for M&A activity to help catalyse revaluations.

Valuation: Narrowing discount, above-average yield

Tetragon's share price discount to NAV has narrowed appreciably over the last 15 months. The current 36.0% discount is lower than its 39.8% five-year average, but remains significantly wider than its five-year low of 20.4%, leaving scope for further narrowing to enhance future shareholder returns. Tetragon's 5.3% dividend yield ranks as one of the highest among its Flexible Investment sector peers.

Investment companies

15 June 2017

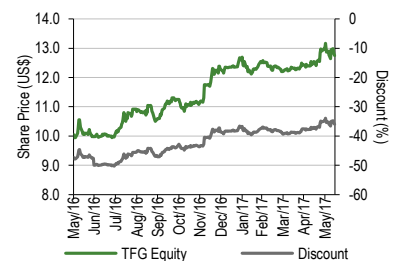
Price US\$12.75
Market cap US\$1,243m
NAV* US\$1,941m

NAV per share* US\$19.92
 Discount to NAV 36.0%

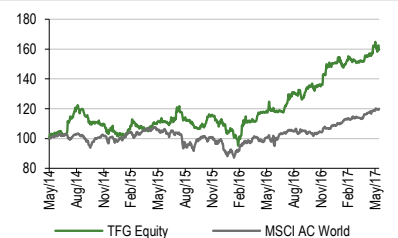
* As at 30 April 2017.

Yield 5.3%
 Fully diluted shares in issue 97.5m
 Code TFG
 Primary exchange Euronext Amsterdam
 Secondary exchange LSE Specialist Fund Segment
 AIC sector Flexible Investment
 Benchmark N/A

Share price/discount performance



Three-year performance graph



52-week high/low US\$13.17 US\$9.95
 NAV** high/low US\$20.12 US\$19.07

Gearing

Gross borrowings* 2.0%
 Net cash* 20.4%

*As at 30 April 2017.

Analysts

Gavin Wood +44 (0)20 3681 2503
 Sarah Godfrey +44 (0)20 3681 2519

investmenttrusts@edisongroup.com

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Exhibit 1: Company at a glance

Investment objective and fund background

Tetragon's investment objective is to generate distributable income and capital appreciation, aiming to provide stable returns to investors across various credit, equity, interest rate, inflation and real estate cycles. Tetragon's investment portfolio comprises a broad range of assets, including a diversified alternative asset management business, TFG Asset Management, and covers bank loans, real estate, equities, credit, convertible bonds and infrastructure.

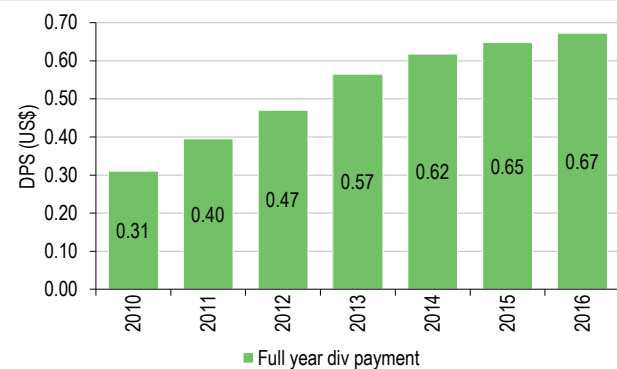
Recent developments

- 27 April 2017: US\$0.1725 Q117 dividend declared vs US\$0.1650 in Q116.
- 21 April 2017: 12.5m options exercised by TFM at US\$10.00 per Tetragon share.
- 2 March 2017: Final results for FY16 – NAV total return +8.5% vs MSCI AC World +8.5% and FTSE All-Share -2.1%, all in US dollar terms.
- 1 March 2017: US\$0.1725 Q416 dividend declared vs US\$0.1650 in Q415; FY16 total dividend US\$0.6725 vs US\$0.6475 for FY15.
- 23 December 2016: IFRS adopted, triggering US\$25.1m performance fee.
- 12 December 2016: US\$50m tender offer – 4.3m shares accepted at US\$11.60 per share.

Forthcoming		Capital structure		Fund details	
Investor day	2018 date TBC	Ongoing charges	1.64%	Group	Tetragon Financial Group
Interim results	31 July 2017	Net cash	20.4%	Manager	Tetragon Financial Management
Year end	31 December	Annual mgmt fee	1.5% of net assets	Address	1st Floor Dorey Court, Admiral Park St. Peter Port, Guernsey GY1 6HJ
Dividend paid	May, Aug, Nov, Mar	Performance fee	25% over Libor+2.65% hurdle	Phone	+44 20 7901 8328
Launch date	19 April 2007	Trust life	Indefinite	Website	www.tetragoninv.com
Continuation vote	N/A	Loan facilities	US\$150m rolling credit facility		

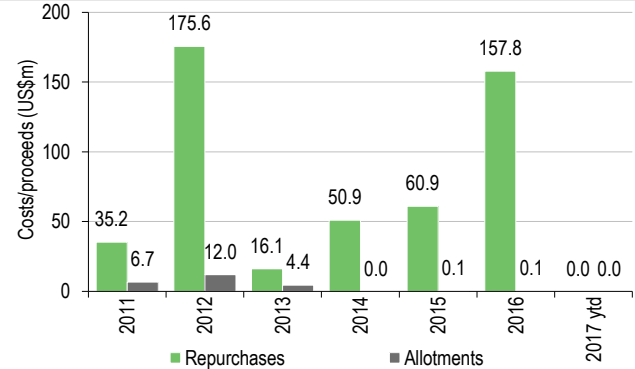
Dividend policy and history

Tetragon pursues a progressive dividend policy with a target payout ratio of 30-50% of normalised earnings. Dividends are paid quarterly.

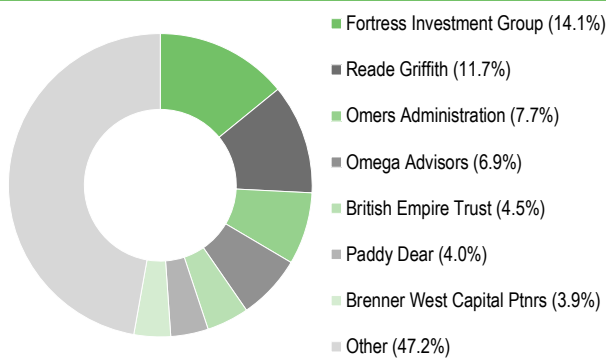


Share buyback policy and history

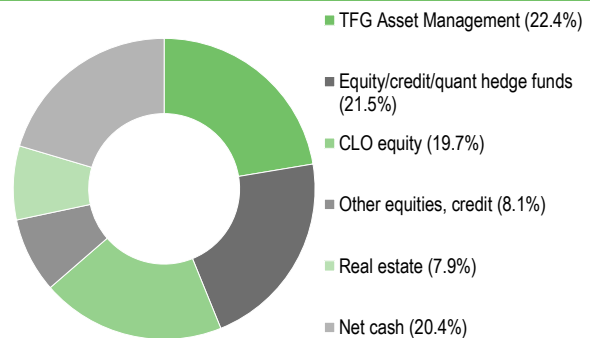
Tetragon made market share repurchases from December 2007 to April 2013 and has completed five tender offers totalling US\$410m since December 2012.



Shareholder base (as at 5 June 2017)



Portfolio exposure by asset class (as at 30 April 2017)



Top 10 holdings (as at 30 April 2017)

Holding	Investment type	Description	% of NAV	
			30 April 2017	31 March 2016**
Polygon European Equity Opportunity Fund	Equities	European event driven equity hedge fund	10.4	7.4
Equitix*	Asset Manager	£2.1bn UK infrastructure fund asset manager	10.1	9.2
Polygon Distressed Opportunities Fund	Credit	Distressed opportunities hedge fund	5.6	4.6
LCM*	Asset Manager	US\$6.6bn CLO manager	5.6	5.1
GreenOak Real Estate*	Asset Manager	US\$7.1bn global real estate asset manager	3.5	3.4
Polygon*	Asset Manager	US\$1.6bn hedge fund manager	3.1	3.1
Polygon Convertible Opportunity Fund	Credit	Event-driven credit hedge fund	2.7	2.3
GreenOak US II Fund	Real Estate	US real estate fund	2.0	N/A
LCM XXIV	CLO Equity	US broadly syndicated corporate loans (CLO)	1.7	N/A
LCM XIX	CLO Equity	US broadly syndicated corporate loans (CLO)	1.5	1.6
Top 10 at each date			46.2	40.4

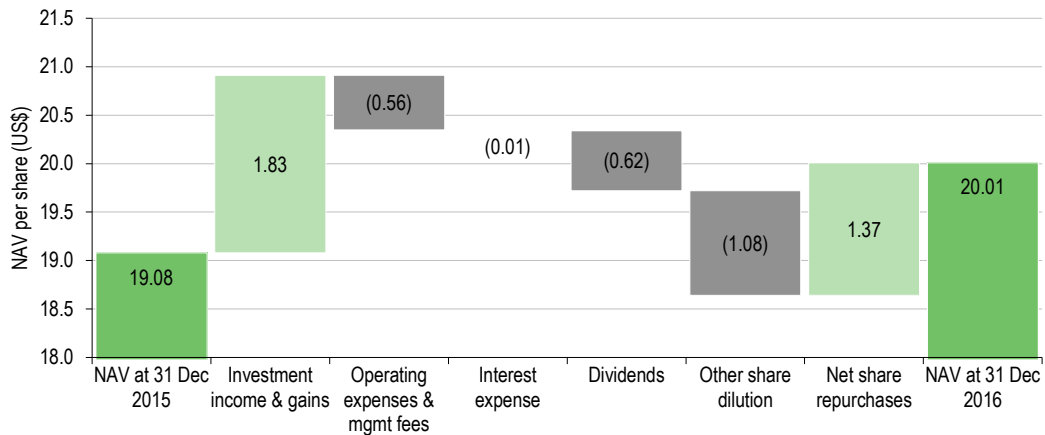
Source: Tetragon Financial Group, Morningstar, Thomson Reuters, Bloomberg, Edison Investment Research. Note: *Part of TFG Asset Management. **April 2016 data not published; N/A where not in March 2016 top 10.

Steady progress made during 2016

Tetragon generated US\$125.9m fair value net income in 2016, equating to an investment return on equity (ROE) of 6.3%. This compares to FY15's reported US\$263.9m net income and 14.5% ROE, with a comparable 8.2% ROE after adjusting for a one-off fair valuation effect. Total NAV declined from US\$1,987.3m to US\$1,934.9m due to US\$203.7m being distributed to shareholders during the year through dividend payments and share repurchases. However, Tetragon's fully diluted NAV per share rose from US\$19.08 to US\$20.01 over the year and its NAV total return for 2016 was 8.5% in US dollar terms.

Exhibit 2 shows the contributors to the US\$0.93 rise in Tetragon's NAV per share, highlighting investment income and gains as the main driver of performance, although the uplift from repurchasing shares at a substantial discount to NAV in two tender offers also made a material contribution. The 24.1% rise in Tetragon's share price during 2016 had a dilutive effect, through increasing the intrinsic value of in-the-money issued share options.

Exhibit 2: Tetragon's fully-diluted NAV per share progression in 2016



Source: Tetragon Financial Group

During 2016, all asset classes made a positive contribution to Tetragon's US\$184.1m gross investment returns. CLO investments recorded gains of US\$99.9m, primarily from US CLOs, which saw older vintages continuing to amortise, early optional redemptions being undertaken and refinancing completed on a number of CLO 2.0 transactions. Equity and credit hedge funds recorded gains of US\$26.4m, with Polygon's Distressed Opportunities and European Equity Opportunity funds the most significant contributors. TFG Asset Management recorded a US\$21.6m underlying gain, principally from Tetragon's second-largest holding, UK infrastructure fund asset manager Equitix, although this was offset by negative foreign exchange effects due to the decline in sterling against the US dollar during the year. The underlying gain was driven by a strong investment performance and asset raising, although in US dollar terms AUM declined from US\$2.8bn to US\$2.5bn over the year. There were mostly small valuation declines across the other asset managers, except for TCIP. Direct investments, principally equities, contributed gains of US\$27.0m. Real estate gained US\$9.0m while there was a US\$0.2m gain on Tetragon's substantial cash position. Total operating expenses were at a similar level to the prior year, with Tetragon reporting a decline in ongoing charges to 1.64% in 2016 from 1.70% in 2015.

Tetragon declared total dividends of US\$0.6725 per share for 2016, 3.9% higher than 2015. Following a similar pattern to previous years, the Q116 and Q316 dividends were held steady while the Q216 and Q416 dividends were increased from the prior quarter.

Tetragon's fully diluted share count declined from 104.2m to 96.7m during 2016. The main element of this change was the 14.3m shares repurchased under the US\$100m and US\$50m tender offers

in June and December. Offsetting factors include the issue of shares to satisfy scrip dividends, an increase in the intrinsic value of in-the-money options resulting from the 24.1% rise in Tetragon's share price over the year, and equity-based compensation awards to certain senior employees of TFG Asset Management (5.1m shares awarded with vesting dates up to 2024).

2017 performance

NAV total return was 1.4% in Q117, with positive returns from all asset classes other than equity and credit hedge funds, where the Polygon Distressed Opportunities Fund recorded a negative performance after expenses. TFG Asset Management delivered the strongest performance, driven by an increase in the fair value of Equitix, mainly reflecting continued delivery against its business plan. CLO investments were helped by an upward move in Libor, while the Polygon European Equity Opportunity Fund and direct equity investments also made significant contributions. TFG Asset Management's AUM rose by US\$0.3m to US\$19.8bn during the quarter.

A marginally negative NAV total return was recorded in April 2017, principally due to a decline in CLO valuations, which were negatively affected by tightening loan spreads. This decline was offset by gains before expenses across all other asset classes, with hedge funds making the largest positive contribution.

Tetragon's fully diluted share count rose from 96.7m at end-2016 to 97.5m at end-April 2017, primarily due to the issue of shares to satisfy scrip dividends. Shortly before their expiry on 26 April 2017, Tetragon's investment manager TFM exercised 12.5m options at US\$10.00 per share (the IPO offer price), which it had been granted in relation to Tetragon's 2007 share offering and associated capital raising. These options were settled on a cashless basis, with 2.4m shares issued based on a price of US\$12.34 per share.

Adoption of IFRS

In December 2016, Tetragon adopted IFRS, resulting in all its investments being carried at fair value in its audited financial statements from end-2016. This simplifies Tetragon's financial reporting as IFRS accounting methodology is equivalent to that used to determine Tetragon's fair value NAV as reported in prior periods. From end-2016, Tetragon is also using IFRS NAV to determine fees payable to the investment manager. The switch to IFRS resulted in an uplift in the NAV of certain TFG Asset Management businesses, triggering a US\$25.1m incentive fee, although the investment manager has agreed to accept deferred payment in the form of 2.0m Tetragon shares. Under IFRS, no liability is recognised for the incentive fee but there is full dilution for the deferred shares. Tetragon had previously accounted for the incentive fee as a liability in its fair value reporting, so the change in accounting treatment results in a US\$25.1m increase in NAV but a US\$0.13 reduction in NAV per share.

New investments

Investment additions (including amounts paid on forward forex hedges) totalled US\$137.6m in 2016, including US\$42.0m in the Polygon European Equity Opportunity fund, US\$35m drawn down by GreenOak real estate funds, US\$15.3m in LCM-managed US CLOs, US\$15.9m drawn down by TCI II (US multi-manager CLO equity), US\$19.1m in direct equity investments and US\$8.3m in direct credit investments. Investment additions amounted to US\$96.5m in Q117, with Tetragon investing US\$33.2m in US CLOs via LCM, making a new US\$25m investment in QT Fund, a quantitative hedge fund managed by Credit Suisse's systematic strategies group, and adding US\$21.6m to direct equity investments (mainly in existing holdings), while US\$12.4m was drawn down by real estate funds. In addition, a capital call was received from Hawke's Point as it made its first investment in an Australian mining company.

Realisations

Realisations (including amounts received on forward forex hedges) amounted to US\$374.0m during 2016, with the most significant proceeds coming from CLO investments, including US\$236.0m from US CLOs and US\$33.9m from European CLOs. Real-estate investment realisations accounted for US\$43.2m, while direct investment realisations amounted to US\$22.5m. TFG Asset Management saw a realisation of US\$32.6m, primarily as a result of realised proceeds on the forward forex contracts hedging the local currency value of the Equitix investment back into US dollars.

Q117 realisations (including foreign exchange movements) totalled US\$122.7m, including US\$79.1m proceeds from CLO investment realisations, principally from US CLOs, US\$9.2m from real estate fund realisations and US\$6.7m from direct equity and credit investment realisations. April 2017 saw US\$36.6m in CLO realisations which, in combination with the weaker performance of its CLO investments over the month, resulted in Tetragon's CLO equity exposure declining below that of both TFG Asset Management and hedge fund investments (see Exhibit 1).

In December 2016, Polygon decided to wind down its US\$69.6m Mining Opportunity Fund, which recorded in a small loss for 2016, in light of its reduced potential to deliver consistent and sustainable returns from a diminished opportunity set. Tetragon (along with all fund investors) expects to receive distributions of cash from its investment in full by the end of 2017. In Q117, Tetragon received US\$27.4m of distributions from the Mining Opportunity Fund, reducing its exposure to 0.5% of NAV.

US\$100m and US\$50m tender offers

Tetragon completed a US\$50m tender offer in December 2016, buying back 4.3m shares at US\$11.60. This followed a US\$100m tender offer in June 2016 under which 10m shares were repurchased at US\$10.00. While the repurchase of shares served to reduce Tetragon's overall net assets, the tender offers were priced at substantial discounts to NAV, making the buybacks meaningfully accretive to NAV per share. In addition to the two tender offers, Tetragon repurchased 0.6m shares held by Michael Humphries, a manager of certain Polygon funds. In total, share repurchases contributed c 7% to Tetragon's 2016 NAV total return, outweighing the c 5% negative effect from share dilution arising from the issue of scrip dividends, equity-based compensation awards and increase in the intrinsic value of in-the-money share options resulting from the rise in Tetragon's share price.

Cash and borrowings

Tetragon continues to maintain a substantial cash position to cover future commitments and also enable it to capitalise on opportunistic investments and new business opportunities. At end-2016, Tetragon held net cash of US\$390.6m, representing 20.0% of net assets, and net cash at end-April 2017 was slightly higher at US\$395.9m (20.4% of NAV). All Tetragon's cash is held at highly rated banking institutions, in on-demand arrangements, to ensure that it is not exposed to any term risk.

Tetragon's management sees the net cash position as close to the optimum level on a 12-month view given its US\$237m end-2016 cash commitments, with US\$90.9m and US\$46.1m investment commitments to GreenOak and TCI II and prospective investments of US\$100m via Hawke's Point, as well as ongoing fees and annual dividend payments of c US\$65m.

In April 2016, Tetragon arranged a US\$75m three-year revolving credit facility, which was increased to US\$150m in August 2016. This facility provides Tetragon with additional flexibility to make opportunistic investments and there is no intention to introduce structural leverage at the corporate level. US\$38.0m was drawn against this facility at end-2016.

Discount: Recent narrowing

As illustrated in Exhibit 3, Tetragon's share price discount to NAV followed a widening trend from March 2013 to February 2016 when the trend reversed and the discount has contracted over the last 15 months. The current 36.0% discount is narrower than its 39.8% five-year average but remains significantly wider than its five-year low of 20.4%, leaving considerable scope for further narrowing to enhance future shareholder returns.

Exhibit 3: Share price discount to NAV over five years (%)



Source: Thomson Datastream, Edison Investment Research

Peer group comparison

Exhibit 4 shows a comparison of Tetragon with the other AIC Flexible Investment sector funds over US\$100m market cap. We no longer include AIC Sector Specialist: Debt sector funds focused on CLO securities in the comparison as Tetragon's CLO equity exposure has declined to less than 20% of NAV at end-April 2017 (see Exhibit 1). Tetragon's NAV total return has significantly outperformed the peer group average over one, three, five and 10 years to end-April 2017, ranking second over one year and first over three, five and 10 years. With Tetragon celebrating its 10th anniversary, we note that it has achieved considerable outperformance of the peer group since its launch in April 2007, delivering an 11.3% pa NAV total return to end-April 2017.

Exhibit 4: Flexible investment sector peer group as at 14 June 2017*

% unless stated	Market cap US\$m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Discount (ex-par)	Ongoing charge	Perf. fee	Net gearing	Dividend yield (%)
Tetragon Financial Group	1,218.3	8.1	31.9	78.1	199.5	(36.0)	1.64	Yes	100	5.3
Aberdeen Diversified Income & Growth	500.5	(4.9)	(19.6)	4.5	(14.6)	(10.8)	0.62	No	105	5.5
Capital Gearing	232.1	(0.3)	(4.4)	8.0	31.0	1.7	1.03	No	100	0.5
Henderson Alternative Strategies Trust	135.3	8.9	(10.7)	(20.2)	(45.1)	(15.5)	1.01	Yes	100	1.4
Personal Assets	1,049.0	(2.7)	(4.0)	2.0	16.2	1.7	0.95	No	100	1.4
RIT Capital Partners	3,758.4	2.3	5.5	28.5	21.0	4.5	1.14	Yes	104	1.6
Ruffer Investment Company	493.3	(0.7)	(9.4)	2.4	48.5	2.3	1.17	No	100	0.8
Syncona	1,275.5	1.4	(2.6)			10.6	1.27	No	100	1.5
Flexible Investment funds average	1,082.8	1.5	(1.7)	14.8	36.6	(5.2)	1.10		101	2.2
Tetragon's rank in peer group	3	2	1	1	1	8	1		3	2

Source: Morningstar, Edison Investment Research. Note: *Performance data to end-April 2017. TR = total return in US\$ terms. Net gearing is total assets less cash and equivalents as a percentage of net assets.

Although it has narrowed by more than 10 percentage points over the last year, Tetragon's share price discount to NAV remains the widest in the peer group, suggesting that factors including lack of investor awareness and perceived lack of share liquidity continue to weigh on the share price.

Tetragon's ongoing charge is the highest in the peer group and it is one of three funds to charge a performance fee. Tetragon's structural cash position means that it has no net gearing, similar to the majority of peers. Tetragon's 5.3% dividend yield is one of the highest in the peer group, significantly ahead of the 2.2% average yield.

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