EDISON

Tetragon Financial Group

Global diversified alternative assets portfolio

Initiation of coverage

Investment companies

Tetragon Financial Group (TFG) is a specialist closed-ended investment company aiming to provide stable returns across economic and various asset class cycles through investing in a selected portfolio of alternative assets. Within each asset class, the manager seeks to outperform through identifying the most appropriate structure for investments, as well as selecting high-quality specialists to manage the underlying investments. Targeting an annual return of 10-15%, TFG's NAV total return has substantially outperformed major equity markets and its peers over one, three and five years, and since the fund's launch in April 2007. Steps are being taken to address a persistently wide discount, which currently substantially enhances the dividend yield on TFG's shares.

12 months ending	Total share price return (%)	Total NAV return (%)	MSCI AC World (%)	FTSE All-Share (%)	US 10y Govt Bond index (%)
31/07/12	2.7	23.2	(3.1)	(4.2)	15.7
31/07/13	49.2	13.3	21.2	20.3	(6.4)
31/07/14	6.7	15.4	16.5	17.6	3.6
31/07/15	5.4	7.6	3.4	(2.6)	5.7
31/07/16	1.7	18.5	0.1	(11.7)	8.6

Note: Twelve-month rolling discrete US dollar-adjusted total return performance up to last reported NAV.

Investment strategy: Selective alternative strategies

Looking to generate distributable income and capital appreciation, TFG's manager seeks uncorrelated, alpha-generating strategies, aiming to identify asset classes offering excess returns relative to their investment risk. Analysis covers risk/reward, correlation, duration and liquidity of potential investments to gauge their appeal and expected effect on the portfolio. While historically TFG's primary exposure was to CLOs (see page 15), which made a strong contribution to performance, the portfolio has more recently evolved to comprise a broad range of alternative investments, including a diversified alternative asset management business, and covers bank loans, real estate, equities, credit, convertible bonds and infrastructure.

Market outlook: Uncertainty prevails

Recent strength has pushed US and UK equity market valuations towards 10-year highs and bond yields are sitting at five-year lows, implying that markets may be susceptible to bouts of volatility, with recent downgrades to global GDP growth forecasts suggesting a more cautious outlook may be appropriate. In this environment, investors may see appeal in a fund aiming to deliver absolute returns from a diversified portfolio of alternative assets.

Valuation: Persistently wide discount enhances yield

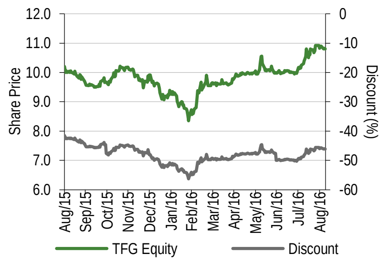
While TFG has achieved a strong performance over the last five years, its share price discount to NAV has remained persistently wide and steps are being taken to address a number of contributory factors. Although seen as a negative, the wide discount enhances the underlying portfolio yield to give TFG shares a 6.1% dividend yield, and provides substantial scope for future shareholder returns to be strengthened by any narrowing of the discount.

12 September 2016

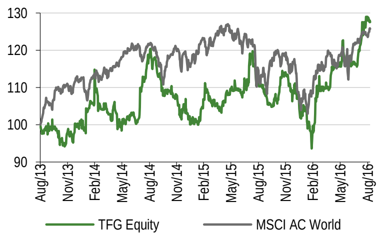
Price	**US$10.80**
Market cap	**US$1,032m**
NAV*	**US$1,919m**

NAV per share*	US$20.06
Discount to NAV	46.2%
*As at 31 July 2016.	
Yield	6.1%
Fully-diluted shares in issue	95.6m
Code	TFG
Primary exchange	Euronext Amsterdam
Secondary exchange	LSE Specialist Fund Segment
AIC sector	Flexible Investment

Share price/discount performance



Three-year cumulative perf. graph



52-week high/low	US$10.92	US$8.35
NAV high/low	US$20.06	US$17.43

Gearing

Gross*	0.0%
Net cash*	21.1%

*As at 31 July 2016.

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Edison profile page

Tetragon Financial Group is a research client of Edison Investment Research Limited

Exhibit 1: Company at a glance

Investment objective and fund background

TFG'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. TFG'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.

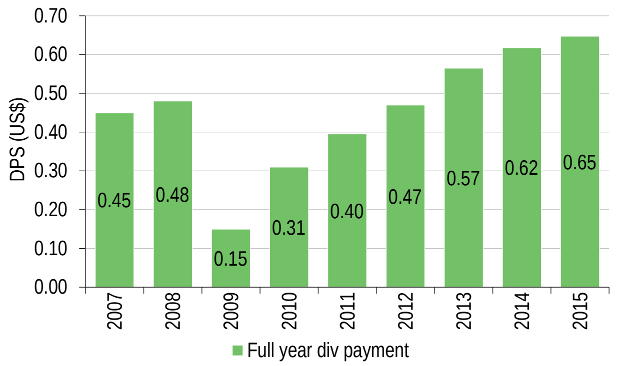
Recent developments

- 29 July 2016: Announced retirement of TFG's CFO Phil Bland later in 2016. He will be succeeded by Paul Gannon, who has been at the firm for 10 years.
- 29 July 2016: Q216 results – NAV total return +3.5% vs FTSE All-Share -2.6%.
- 28 July 2016: US$0.1675 Q216 dividend declared vs US$0.1625 for Q215.
- 14 June 2016: William Rogers appointed as a director, replacing Byron Knief, who stepped down from the board after more than 10 years' service.
- 9 June 2016: Tender offer acceptances confirmed for 10.0m non-voting shares at US$10.00 per share.

Forthcoming		Capital structure		Fund details	
Investor day	8 March 2017	Ongoing charges	1.75% (see page 12)	Group	Tetragon Financial Group
Quarterly results	31 October 2016	Net cash	21.1%	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 hurdle (see page 12)		
Launch date	Aug 2005 (listed 19 April 2007)	Company life	Indefinite	Phone	+44 20 7901 8328
Continuation vote	N/A	Loan facilities	US$75m rolling credit facility	Website	www.tetragoninv.com

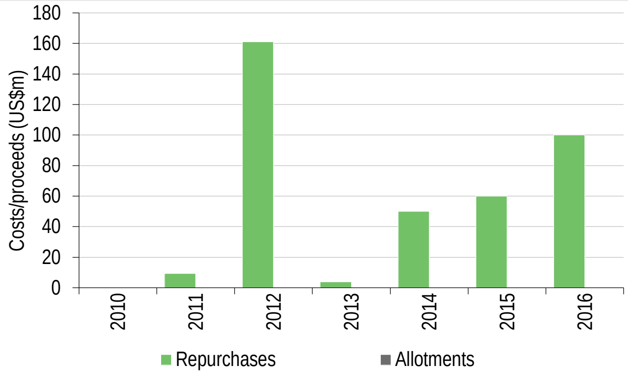
Dividend policy and history

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

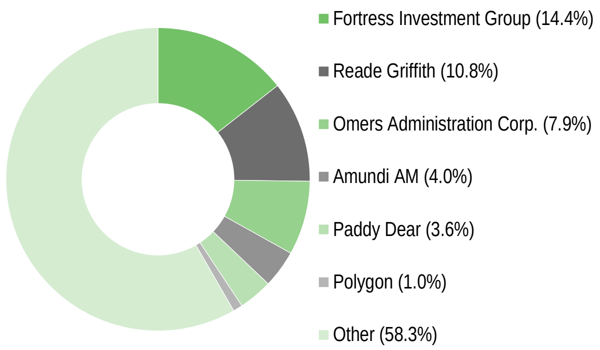


Share buyback policy and history

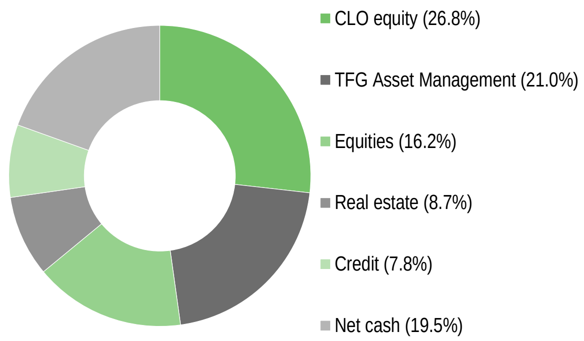
Since launch, TFG has bought back 57.1m shares at a cost of US$486.2m through market purchases and tender offers. US$60m and US$100m tender offers were completed in December 2015 and June 2016.



Shareholder base (as at 28 June 2016)



Portfolio exposure by asset class (as at 30 June 2016)



Top 10 holdings (as at 30 June 2016)

Holding	Investment type	Description	% of fair value NAV	
			30 June 2016	31 December 2015**
Equitix*	Asset manager	£1.9bn UK infrastructure fund asset manager	8.8	8.7
Polygon European Equity Opp. Fund	Equities	European event-driven equity hedge fund	7.8	7.0
LCM*	Asset manager	US$6.4bn CLO manager	5.4	5.5
Polygon Distressed Opp. Fund	Credit	Distressed opportunities hedge fund	5.0	4.8
GreenOak Real Estate*	Asset manager	US$6.8bn global real estate asset manager	3.5	3.5
Polygon*	Asset manager	US$1.5bn hedge fund manager	3.3	3.4
Polygon Convertible Opportunity Fund	Credit	Event-driven credit hedge fund	2.5	2.2
Polygon Mining Opportunities Fund	Equities	Mining related equity hedge fund	2.2	1.9
LCM XVI LP	CLO equity	US broadly syndicated corporate loans (CLO)	1.9	1.5
GreenOak US II Fund	Real estate	US real estate fund	1.9	N/A
Top 10			42.3	40.3

Source: Tetragon Financial Group, Morningstar, Thomson, Bloomberg, Edison Investment Research. Note: *Part of TFG Asset Management. **N/A where not in December 2015 top 10.

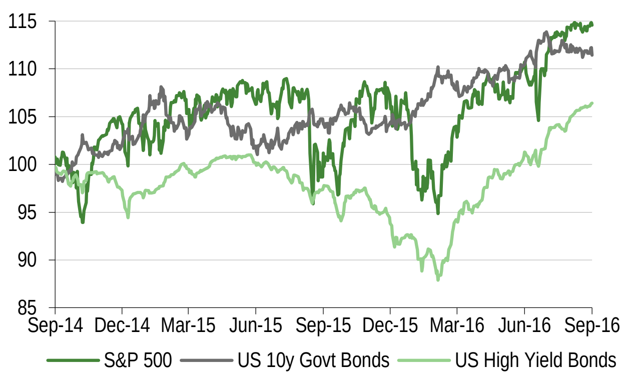
Market outlook: Alternative assets may appeal

In an environment of volatile equity markets and declining bond yields, investors may wish to consider alternative asset classes as a potential source of uncorrelated returns. As illustrated in Exhibit 2 (left-hand chart), while US equities, government and corporate bonds have all delivered positive returns in 2016, with the S&P 500 Index reaching new highs, markets have witnessed increased volatility over the last two years, with notably sharp falls in the S&P 500 Index seen in August 2015 and January 2016, influenced by global macroeconomic uncertainties. The recent strength of bond markets has seen government bond yields fall to new five-year lows (see Exhibit 2 right-hand chart) and pushed the yield premium of equities relative to bonds close to its highest level over the last 10 years, increasing the relative appeal of equities as an asset class.

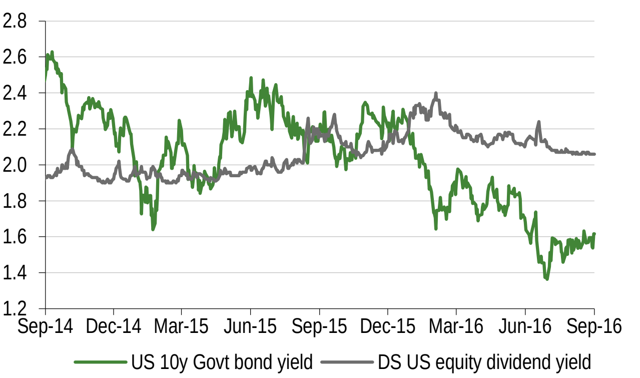
Although dividend yields across developed equity markets remain similar to 10-year average levels, recent market strength has pushed forward P/E multiples for the US and UK stock markets close to 10-year highs. Seemingly reduced scope for valuation multiples to expand further makes earnings growth appear the most likely primary driver for markets to move higher and, with global economic growth projections recently being lowered, this suggests that markets may be susceptible to further bouts of volatility if corporate earnings fall short of market expectations.

Exhibit 2: US equity returns vs government and corporate bonds over two years

S&P 500 Index returns versus US government and corporate bonds



US 10-year government bond yield versus US equities dividend yield



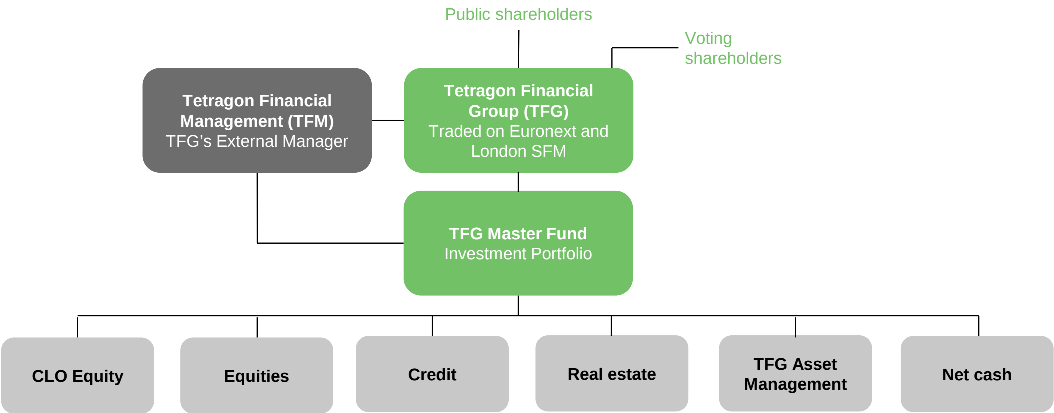
Source: Thomson Datastream, Edison Investment Research

US and UK stock market valuations sitting at close to 10-year highs, US government bond yields at five-year lows and recent downgrades to global GDP growth forecasts suggest a more cautious outlook may be appropriate across equity and debt markets. In addition, a wide range of global macroeconomic uncertainties exist, which could contribute to elevated levels of market volatility persisting in the near term. In this environment, investors may see appeal in a fund aiming to deliver absolute returns from a diversified portfolio of alternative assets.

Fund profile: Global alternative assets portfolio

Tetragon Financial Group is a Guernsey-domiciled closed-ended company founded in August 2005. TFG's shares were admitted to trading on Euronext Amsterdam in April 2007 and since November 2015 have also been listed on the Specialist Fund Segment of the London Stock Exchange. TFG'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. The 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. TFG currently invests through a structure whereby TFG's only direct investment is in shares of the TFG Master Fund (see Exhibit 3).

Exhibit 3: TFG group structure



Source: Tetragon Financial Group, Edison Investment Research

Tetragon Financial Management (TFM) has been TFG's investment manager since its launch. TFM is controlled by Reade Griffith and Paddy Dear, co-founders of TFG and Polygon, who also control TFG's voting shares. TFM's Investment Committee currently consists of Griffith, Dear, Jeffrey Herlyn, Michael Rosenberg, David Wishnow and Stephen Prince. The Investment Committee determines TFG's investment strategy and approves each significant investment. Since its inception, TFM has used Polygon (now part of TFG Asset Management) to provide a broad range of administrative services as well as services relating to the dealing in and management of investments, arrangement of deals and advising on investments.

TFG's investment strategy can be represented by the following four stages:

- Identification of attractive asset classes and investment strategies.
- Identification of asset managers believed to possess superior skill and experience.
- Negotiation of favourable terms for investments using TFM's market experience.
- Where appropriate, to seek to own all, or a portion, of asset management companies with which it invests, in order to enhance the returns achieved on its capital.

In addition, TFM seeks to continue to grow TFG's diversified alternative asset management business, TFG Asset Management, with a view to a possible initial public offering.[1]

Having focused on debt markets from its launch in 2005, in particular collateralised loan obligations (CLOs – see Appendix: Collateralised loan obligations (CLOs)), which made a strong contribution to performance, TFG has substantially diversified its portfolio since 2010, currently deploying its capital across the following alternative asset classes:

- CLO equity – comprising investments in US CLO 1.0 (issued pre-financial crisis), US CLO 2.0 (issued post-financial crisis) and European CLOs. The portfolio currently consists of 65 CLOs, each with a pool of c 120 underlying loans.
- Equities – comprising investments in equity hedge funds managed by Polygon and other directly held equity investments.[2]
- Credit – comprising investments in a convertible bond hedge fund and a distressed debt hedge fund managed by Polygon, as well as direct credit investments.
- Real estate – comprising investments in c 10 funds, each with multiple underlying holdings.
- Asset management – comprising investments in six unlisted asset managers, each specialising in a niche alternative investment strategy.

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1 TFM aims to grow TFG Asset Management, as TFG's alternative asset management business, with a view to a planned initial public offering and listing of its shares in the next three to five years.

2 Directly held equities managed by TFM typically represent c 5% or less of TFG's NAV. TFG directly held a 30% stake in Ashcourt Rowan before its takeover by Towry in May 2015.

TFG Asset Management

As shown in Exhibit 4, TFG's asset-management platform currently consists of LCM, GreenOak, Polygon, Equitix, Hawke's Point, TCIP and TCICM. Majority stakes are held in all of the businesses except the GreenOak joint venture and TCICM, which is a subsidiary of the TCI II fund managed by TCIP. As with other investment categories, TFM is responsible for acquisitions and disposals of asset management businesses, but following acquisition these businesses become part of TFG Asset Management, which seeks to generate income and enhance value through growing assets under management (AUM) attributable to third-party investors. TFG Asset Management's role includes oversight of the individual businesses as they form and grow. TFG may invest in funds managed by a TFG Asset Management business and also provide financial support to any fund, where it will benefit from value creation through its stake in the business.

Exhibit 4: TFG Asset Management businesses as at 30 June 2016

	Description	Asset class	Funds managed	AUM (US$bn)	TFG's investments in funds (US$m)
LCM Asset Management	CLO loan manager	Bank loans	14 CLOs	6.4	227.9
GreenOak joint venture	Real estate-focused principal investing, lending and advisory firm	Real estate	Japan Fund I Asia Fund II UK Debt Fund I Europe Fund I Spain US Funds I & II Global Advisory	6.8	138.3
Polygon Global Partners	Manager of open-ended hedge fund and private equity vehicles across a number of strategies	Hedge funds, private equity	European Equity Opportunity Fund Convertible Opportunity Fund Mining Opportunity Fund Global Equities Fund Distressed Opportunities Fund Recovery Fund	1.5	352.7
Equitix	Integrated core infrastructure asset management and primary project platform	Infrastructure	Fund I, II, III & IV Managed Account Energy Saving Investments Energy Efficiency Fund	2.6	18.5 (indirect exposure)
Hawke's Point	Business that seeks to provide capital to companies in the mining and resource sectors	Mining finance	N/A	Start-up	0.0
Tetragon Credit Income Partners (TCIP)	General partner of a private equity vehicle that invests in CLOs in accordance with risk-retention rules	CLO equity	Tetragon Credit Income II (TCI II) TCI Capital Management	0.2	50.0
TCI Capital Management (TCICM)*	CLO loan manager	Bank loans	First CLO closed in July 2016	0.3	0.0
				17.8	768.9

Source: Tetragon Financial Group, Edison Investment Research. Note: *TCICM is a subsidiary of TCI II.

The fund manager: Tetragon Financial Management

The manager's view: Growth expected to continue through 2016

During 2015, which was seen as a challenging year for many investment strategies and a difficult market environment as a whole, the manager considers that TFG made a number of significant achievements. These included TFG posting strong annual return on equity (ROE) growth, both on a like-for-like basis and on a fair value basis, while TFG Asset Management continued to grow through active capital raising into existing businesses, launch of new businesses and acquisitions. Several important initiatives were also undertaken to enhance shareholder value.

The manager's view is that performance across asset classes was generally negative throughout the investment industry during 2015 and H116, with positive returns in many cases only modest. Against that backdrop, TFG's 16.0% NAV total return in 2015 was seen as a creditable performance, with all but one of TFG's asset classes and underlying investment strategies posting positive returns. This compares with negative returns across the leveraged finance market, evidenced by the Credit Suisse Leveraged Loan and Distressed Loan indices returning -0.38% and -25.9%, respectively, in 2015. TFG Asset Management, US CLOs, European event-driven equities and global real estate investments, in particular, delivered strong positive performances. TFG reported a 14.5% fair value ROE in 2015, including 6.3% attributable to the first time inclusion at fair value of certain TFG Asset Management businesses (LCM, Polygon and Hawke's Point) reflecting value creation over three years, while the underlying ROE was 8.2%.

As announced in 2015, TFG is continuing to grow TFG Asset Management with a view to a planned initial public offering of the asset management business in the next three to five years. To that end, TFG Asset Management continues to increase EBITDA and grow assets under management, with the underlying investment strategies predominantly delivering a positive performance and new managers being added to the platform.

The manager comments that unprecedented monetary easing has been witnessed over the past several years resulting in historically low interest rates globally, noting that although TFG may achieve lower sustainable returns in low-Libor environments, it is generally invested in strategies that are seeking absolute rather than relative returns. TFG's performance in 2015 is believed to reflect this approach. Throughout 2016, the manager expects that the asset classes and investment strategies represented in TFG's portfolio will continue to produce what are considered to be uncorrelated returns. The aim for TFG Asset Management is to continue to grow AUM and profitability, with the manager continuing to look for new asset classes and new asset managers to add to the platform.

Asset allocation

Investment process: Uncorrelated, alpha-generating strategies

To achieve TFG's investment objective of generating distributable income and capital appreciation, TFM focuses on alternative asset classes, seeking uncorrelated, alpha-generating strategies. TFM seeks to identify asset classes that offer excess returns relative to their assessed investment risk, or intrinsic alpha. Analysis covers the risk/reward, correlation, duration and liquidity characteristics of each potential investment to gauge its attractiveness and expected incremental effect on the portfolio. This approach has resulted in TFG's portfolio evolving to comprise a range of alternative investment strategies that would not be easy for investors to access directly.

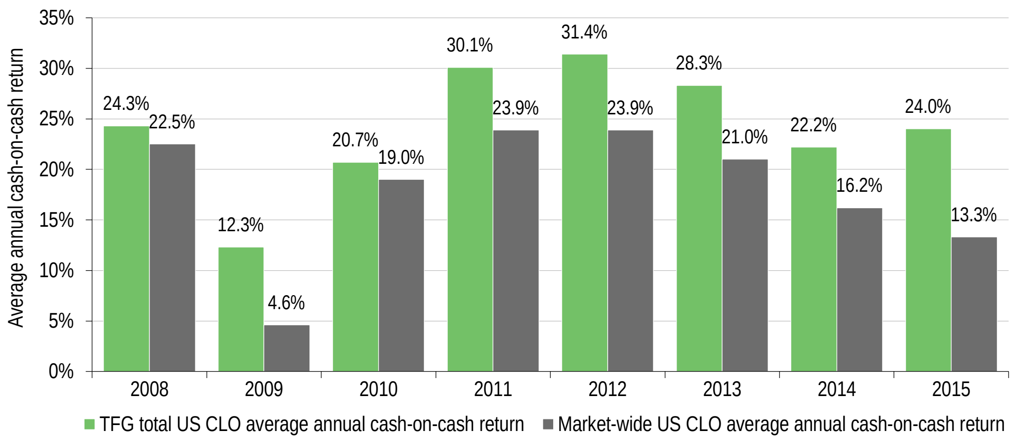
Exhibit 5: Polygon funds' performance versus benchmark peer group indices

Fund	Description	AUM (US$m)	TFG investment (US$m)	Fund H116 return	Fund inception	Fund annualised net performance since inception	Benchmark index	Index H116 return	Index annualised net performance since inception
Convertibles	Primarily investing in North American and European convertible securities	442.3	46.9	4.1%	20 May 2009	16.4%	HFRX Convertible Arbitrage	1.5%	4.9%
European event-driven equity	Primarily investing in major European equity markets with an event-driven focus	649.4	148.0	5.0%	8 July 2009	11.1%	HFRX Event Driven	3.3%	2.1%
Mining equities	Primarily investing in the equities of global gold mining companies	79.9	42.5	12.2%	1 June 2012	5.8%	GDXJ Junior Gold Miners	121.8%	-13.6%
Distressed opportunities	Focused on opportunities in companies undergoing, or about to undergo, balance sheet restructuring	100.3	95.3	2.0%	2 Sept 2013	4.3%	HFRX Distressed Restructuring	7.4%	-1.1%
Global equities		22.7	20.0	1.9%	12 Sept 2011	14.7%	N/A	N/A	N/A
		1,294.8	352.7						

Source: Tetragon Financial Group, Edison Investment Research. Note: Excludes Polygon's private equity vehicle (AUM: US$240.0m).

Once an attractive asset class is identified, TFM looks for high-quality specialist managers who invest in these asset classes and strategies. TFM assesses the range of potential investment vehicles that could be utilised, then selects or structures the one deemed most suitable to optimise TFG's risk-adjusted returns. To highlight the advantage that can be gained by this two-faceted approach, the manager points to the superior returns achieved by TFG's US CLO equity strategy compared with the wider US CLO market. As shown in Exhibit 6, US CLOs delivered positive average annual cash-on-cash returns[3] in each year from 2008 to 2015, although witnessing a sharp decline in return immediately following the global financial crisis, with TFG's US CLO equity strategy outperforming the market in each year.

Exhibit 6: TFG US CLO equity average annual cash-on-cash return versus market



Source: Tetragon Financial Group, Edison Investment Research

Where appropriate, TFM also seeks the opportunity for TFG to take a stake in the asset manager, aiming to produce asset level returns and enhance these returns through exposure to the income stream generated by the underlying asset management businesses. Similar to a private equity or venture capital investor, TFG uses its balance sheet and experience to facilitate these unlisted businesses in growing their funds under management attributable to external investors.[4]

Certain considerations when evaluating the viability of a potential asset manager typically include: performance track records, reputation, regulatory requirements, infrastructure needs and asset gathering capacity. Potential profitability and scalability of the business are also important factors. Additionally, the core capabilities, investment focus and strategy of any new business should offer a complementary operating income stream to TFG Asset Management's existing businesses. TFM looks to mitigate potential correlated risks across investment managers by diversifying exposure across asset classes, investment vehicles, durations, and investor types, among other factors.

From an operational perspective, each of TFG's individual asset management businesses may operate independently or utilising TFG Asset Management's wider resources. In either case, the objective is for them to benefit from an established infrastructure, which can assist in critical business management functions such as risk management, investor relations, financial control, technology, and compliance/legal matters, while maintaining entrepreneurial independence.

As part of its investment strategy, TFM may employ hedging strategies and leverage in seeking to provide attractive returns while managing risk. However, based on the current portfolio profile, TFM deems it appropriate for TFG to hold a net cash position cash representing c 20% of fair value net asset value. This cash balance is held to fund cash flow commitments for existing investments and new investments, as well as dividends,[5] fees payable to TFM and other potential uses of cash.

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[3] Cash-on-cash return reflects returns on invested capital rather than initial investment or capital commitment.

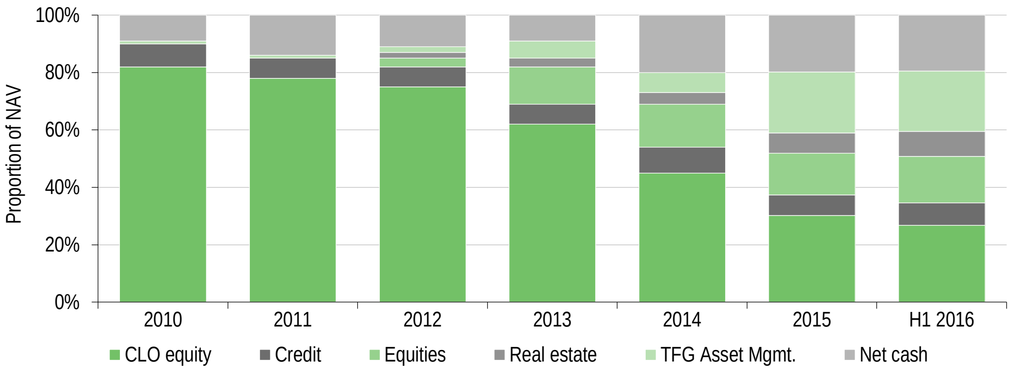
[4] At end-June 2016, TFG accounted for US$769m of TFG Asset Management's total US$17.8bn AUM. The majority of TFG's US$267m investments not managed by TFG Asset Management businesses are CLO equity investments made prior to TFG acquiring LCM.

[5] Dividends are paid out of total net income rather than only revenue earnings.

Current portfolio positioning

While retaining a significant exposure to CLO equity (see Appendix: Collateralised loan obligations (CLOs)), TFG has substantially diversified its portfolio across asset classes since 2010 when CLO equity represented over 80% of its NAV, as illustrated in Exhibit 7. Having focused on debt markets from its launch in 2007, the first investments in asset managers were made in 2010, while equity strategies were introduced to the portfolio along with the acquisition of Polygon in 2012. Over subsequent years, CLO equity exposure has steadily reduced, while exposure to equity, credit and real estate strategies and asset management businesses has broadened.

Exhibit 7: Progression of TFG's net asset exposure by asset class 2010 to H116



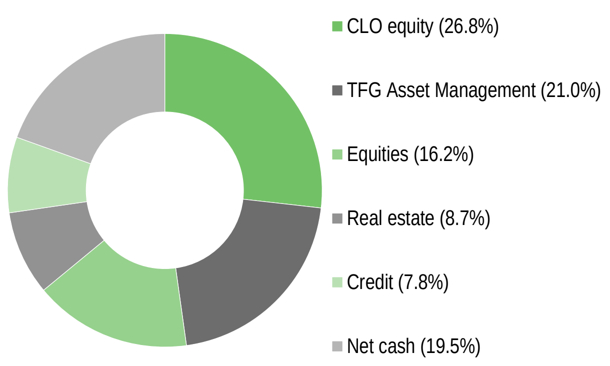
Source: Tetragon Financial Group, Edison Investment Research

During 2015, there was a significant reduction in exposure to CLO equity, reflecting the maturing of existing investments and limited supply of attractive CLO equity investment opportunities, largely offset by an increase in exposure to TFG Asset Management (see Recent developments below). These represent the two largest asset class exposures, representing close to 50% of NAV or c 60% of the invested portfolio at end-June 2016. Net cash has remained at c 20% since end-2014 and stood at 19.5% of NAV at end-June 2016, following the US$100m June 2016 tender offer.

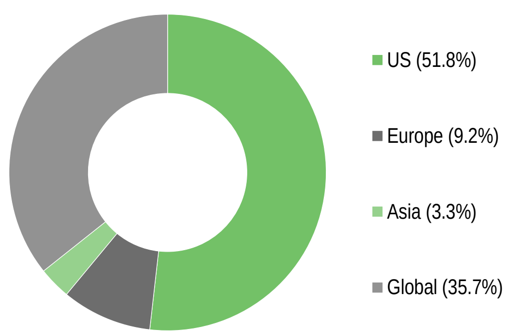
As well as being diversified by asset class, manager and underlying investment, TFG's portfolio is broadly diversified by geography, as illustrated in Exhibit 8. The main change in geographic exposure over the year to 30 June 2016 was a 7.3pp reduction in US exposure, offset by a 7.1pp increase in global exposure.

Exhibit 8: Portfolio fair value analysis by asset class and geography

Fair value net assets split by asset class as at 30 June 2016



Fair value net asset split by geography as at 30 June 2016

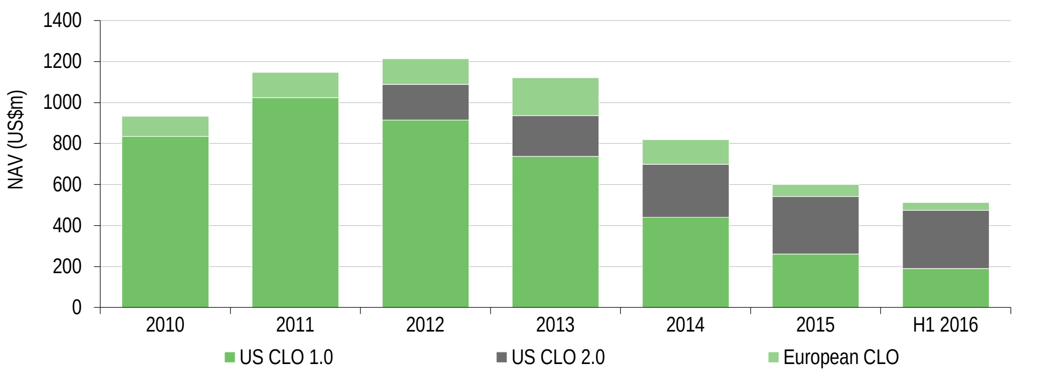


Source: Tetragon Financial Group, Edison Investment Research. Note: Geographic exposure excludes TFG Asset Management.

Recent developments

As shown in Exhibit 9, 2015 marked a turning point in TFG's CLO investing, with the value of portfolio investments in post-financial crisis CLO 2.0 deals rising above pre-financial crisis CLO 1.0 investments, as TFG continued to invest in new CLO 2.0s while CLO 1.0s continued to amortise.

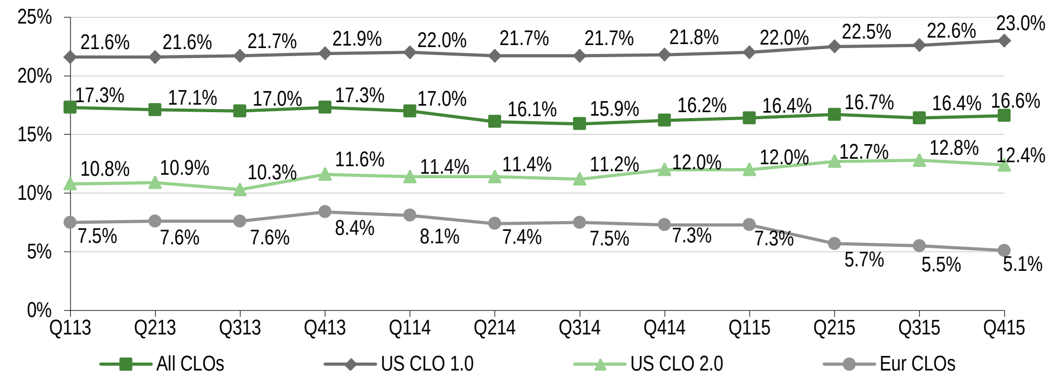
Exhibit 9: Progression of TFG's CLO equity exposure 2010 to H116



Source: Tetragon Financial Group, Edison Investment Research

As outlined in Appendix: Collateralised loan obligations (CLOs), CLO equities proved resilient during the 2008 financial crisis and subsequently generated enhanced returns as the market recovered and loan defaults declined, which explains the superior returns delivered by TFG's CLO 1.0 investments compared with its CLO 2.0 investments, illustrated in Exhibit 10.

Exhibit 10: Weighted average IRR on TFG's CLO investments 2013 to 2015



Source: Tetragon Financial Group, Edison Investment Research

In 2015, TFG acquired majority equity positions in two LCM-managed CLOs for US$62.4m and made a capital commitment of US$35.0m to Tetragon Credit Income II (TCI II), a new vehicle focused on CLO investment that complies with risk-retention rules coming into effect at end-2016, for which TCIP acts as the general partner. TCI II subsequently made its first investment into LCM XX LP. Investments totalling US$81.4m were made into various real estate funds and vehicles across the Americas, Europe, and Asia. TFG also completed the acquisition of 85% of Equitix Holdings for a total enterprise value of £159.5m.

2015 saw TFG sell one US CLO 1.0 transaction for total proceeds of US$6.5m. In addition, optional call rights were exercised on 11 US 1.0 CLOs, generating unwind proceeds of US$67.1m. Certain of these transactions had not liquidated all of their underlying assets before the year end and additional proceeds were received in 2016. An optional early redemption of two European CLOs was initiated, which generated partial unwind proceeds of €23.1m. Additional liquidation payments were received in 2016. US$49.7m was received from return of capital and income on certain investments in GreenOak-managed real estate vehicles, of which US$2.9m was received in 2016.

During 2015, TFG Asset Management's aggregate AUM grew 54% to US$17.1bn, with significant contributions from LCM, GreenOak and Equitix, while the underlying funds managed by the TFG Asset Management platform generally performed well. Two new businesses were added through completing the acquisition of Equitix, an integrated core infrastructure asset management and primary project platform, and launching Tetragon Credit Income Partners (TCIP), the general partner of a private equity vehicle that invests in CLOs in accordance with risk-retention rules requiring CLO managers to hold 5% of their fund. These rules currently apply in Europe and come into force in the US in December 2016. As a core investor in the vehicle, TFG committed US$35m of the US$142.9m total committed capital at the first close in November 2015. By investing alongside third-party investors in one or more TCIP private equity vehicles, TFG has the potential to further diversify its CLO equity holdings across multiple CLO managers, while also benefiting from the value created through TCIP growing its fee income.

Fair value net asset value reporting of TFG Asset Management

TFG presents financial metrics and performance information using a consistent fair-value basis for all of TFG Asset Management. Third-party valuation specialists are engaged by TFG's independent directors to determine indicative valuations for each business and these are used in TFG's fair-value metrics. Exhibit 11 shows the valuation approach for each business and the range of market metrics utilised in determining fair value.

Exhibit 11: Valuation approach to TFG's investments in TFG Asset Management at 30 June 2016

Investment	TFG holding	Fair value (US$m)	% of TFG's NAV	Valuation approach	Discount rate	Valuation multiple	Value as % of manager's AUM
Equitix	75% plus debt	167.1	8.8	Discounted cash flow analysis and cross-check to quoted market multiples. Debt at par + accrued interest	9.5% 15% DLOL	5.5x-6.5x EBITDA 20% discount built-in	N/A
GreenOak	23%	66.0	3.5	Quoted market multiples and cross-check using blended EBITDA and quoted market multiples	N/A	12.0x Adjusted EBITDA	N/A
LCM	100%	102.8	5.4	Discounted cash flow analysis, cross checked to market multiples	10.7-12.7% 15% DLOL	N/A	1.4-1.9% DLOL built-in
Polygon	100%	62.9	3.3	Discounted cash flow analysis and cross-check to quoted market multiples	11.7-13.7% 20% DLOL	6.8x-7.6x EBITDA DLOL built-in	3.3-3.8% DLOL built-in
Hawke's Point	100%	0.7	0.0	Replacement cost approach	N/A	N/A	N/A
TCIP	100%	0.4	0.0	Discounted cash flow analysis	11.6-13.6% 15% DLOL	N/A	N/A
		400.1	21.0				

Source: Tetragon Financial Group, Edison Investment Research. Note: DLOL = discount for lack of liquidity.

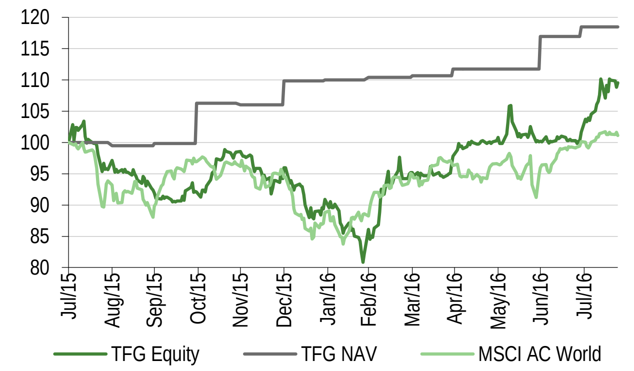
Performance: Outperforming equity markets

While TFG targets an absolute return of 10-15% pa and does not seek to measure its performance against any equity benchmark, comparison with the MSCI AC World Index is considered relevant from a long-term perspective. As shown in Exhibit 13, in US dollar terms, TFG's NAV total return has substantially outperformed the MSCI AC World Index over one, three and five years to end-July 2016, and since TFG's listing in April 2007. The strong performance in June 2016 largely reflected the uplift to TFG's NAV from the US$100m tender offer, priced at a 48% discount to NAV. TFG's NAV has also significantly outperformed the FTSE All-Share Index, over one, three and five years, and since TFG's inception, with the 5.6% decline of the index in June in US dollar terms caused by sterling weakness, augmenting TFG's relative performance over three months. As illustrated in Exhibit 12, while TFG's NAV returns over the last year do not show any particular correlation to the MSCI AC World Index, as would be expected given its absolute return approach, TFG's share price has followed a similar pattern, although significantly outperforming the index. Since its listing in April 2007, in US dollar-terms, TFG has delivered a compound NAV total return of 12.0% pa compared with a 3.5% pa return for the MSCI AC World Index. Exhibit 14 illustrates the relatively consistent nature of TFG's outperformance of the MSCI AC World Index since the 2008 global financial crisis.

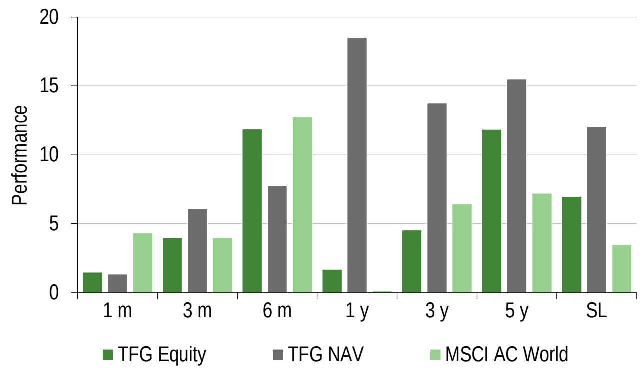
In H116, TFG's NAV total return was 6.4%, with noteworthy positive performance from CLOs and equity hedge funds. TFG Asset Management saw a slightly negative return, primarily due to a more conservative valuation approach being applied, while each individual business saw stable or increasing underlying AUM during the period. Reviewing 2015, the manager notes that both CLO 1.0 and CLO 2.0 investments performed well, delivering US$55.7m and US$30.2m of TFG's US$263.9m fair value net income for the year, with European CLOs also delivering positive returns. To give this performance some context, we note that 2015 saw negative returns across the leveraged finance market, with the Credit Suisse Leveraged Loan and Distressed Loan indices returning -0.38% and -25.91% respectively, while Carador Income Fund, managed by GSO/Blackstone (which invests in CLO equity and debt), reported a -9.7% NAV total return. In a year that was difficult for many hedge funds, the event-driven hedge fund strategy generated double-digit returns, which the manager saw as a strong endorsement of the capabilities of the investment managers selected by TFG. Global real estate also made a positive contribution, leaving the distressed debt strategy as the only negative performer, down 2.2% for the year.

Exhibit 12: Investment company performance to 31 July 2016 in US dollar terms

Price, NAV and index total return performance, one-year rebased



Price, NAV and index total return performance (%)



Source: Thomson Datastream, Morningstar, Edison Investment Research. Note: Three and five-year and SL (since listing) performance figures annualised. Listing date is 19 April 2007.

Exhibit 13: Share price and NAV total return performance relative to indices (%)

	One month	Three months	Six months	One year	Three years	Five years	Since listing
Price relative to MSCI AC World	(2.7)	(0.0)	(0.8)	1.6	(5.2)	23.7	36.1
NAV relative to MSCI AC World	(2.9)	2.0	(4.4)	18.3	22.0	45.1	108.9
Price relative to FTSE All-Share	(1.8)	6.5	6.8	15.1	12.9	50.2	85.6
NAV relative to FTSE All-Share	(1.9)	8.7	2.9	34.2	45.4	76.2	184.9
Price relative to US 10y Govt Bond index	1.2	0.6	6.3	(6.4)	(3.9)	36.0	5.8
NAV relative to US 10y Govt Bond index	1.0	2.6	2.4	9.1	23.7	59.5	62.5

Source: Thomson Datastream, Morningstar, Bloomberg, Edison Investment Research. Note: Data to end-July 2016. Geometric calculation. Listing date is 19 April 2007.

Exhibit 14: NAV performance relative to MSCI AC World since listing

Source: Thomson Datastream, Morningstar, Edison Investment Research

Discount: Persistently wide; scope to narrow

While TFG has delivered a strong NAV total return performance over the last five years, its share price discount to NAV has remained persistently wide, although moving in a relatively broad range. A lack of investor awareness of TFG may be a significant factor behind the wide discount, along with a perceived lack of share liquidity. Other possible factors that may be influencing the discount include the lower level of transparency for a fund holding unlisted investments with valuations published periodically, along with the perceived risk of TFG's investment in both funds and the managers of those funds, the apparent significant influence of the co-founders, TFG's capital structure with voting and non-voting share classes and the level of performance fees.

Recent steps taken to address the wide discount include the admission of TFG's shares for trading on the LSE's Specialist Fund Segment in November 2015, with the aim of improving the liquidity of the shares, as well as US$60m and US$100m tender offers in December 2015 and June 2016. We note that, since listing on the LSE in November 2015, the average daily traded volume of TFG's shares across the London and Amsterdam exchanges and the US OTC market has been c 130,000 shares compared with c 95,000 over the previous 12 months. While TFG has historically made market repurchases of its shares, no share buyback programme has been in place since April 2013. Four tender offers totalling US$360m have been completed since December 2012.

As illustrated in Exhibit 15, over the last five years, TFG's share price discount to NAV has ranged between 20% and 56%, averaging 41%. Over the last 12 months, the discount has moved in a narrower 41% to 56% range, and the current discount is at a similar level to the 12-month average of 48%, leaving substantial scope for a narrowing discount to strengthen future shareholder returns.

Exhibit 15: Share price discount to NAV over five years (%)

Source: Thomson Datastream, Morningstar, Edison Investment Research

Capital structure and fees

TFG has two classes of shares in issue, comprising 10 voting shares and 139.1m non-voting shares. Following the June 2016 tender offer, 12.0m non-voting shares are held in treasury, 27.0m are held by a subsidiary and 12.7m are held in escrow accounts, leaving 87.5m non-voting shares outstanding. On a fully diluted basis, there are 95.6m non-voting shares outstanding, after adjusting for 6.8m escrow shares used as consideration in the 2012 Polygon transaction, 0.5m equity-based awards and 0.9m share options. The 10 voting shares are controlled by TFG co-founders Reade Griffith and Paddy Dear, who also hold significant stakes in TFG's non-voting shares (see Exhibit 1). In total, principal and employee holdings of TFG's non-voting shares (including through equity-based awards) represent approximately 23% of the outstanding shares.

Voting shares give entitlement to vote on the election of board directors and on all other matters, but are not eligible to receive dividends. Non-voting shares do not have any voting entitlement, but carry a right to dividends and other distributions. The escrow shares used as consideration for the Polygon acquisition and related stock dividends are expected to be released over the next two years. 5.8m of the 6.0m TFG shares acquired in the December 2015 tender offer are being held in treasury to meet grants of shares under long-term incentive compensation awards by TFG Asset Management for certain long-standing and senior employees.

In relation to TFG's 2007 share offering and associated capital raising, TFM was granted 12.5m non-voting share options at an exercise price equal to the IPO offer price (US$10.00 per share). These options vested on TFG's admission to Euronext Amsterdam and remain exercisable until 26 April 2017; none has yet been exercised.

TFG does not employ gearing at the corporate level and held cash representing 19.5% of fair value NAV at end-June 2016. Similar to private equity investment companies, partly due to the illiquid nature of the underlying investments, TFG maintains a structural net cash position. This cash balance is held to fund not only existing investment commitments but also new investments, as well as dividends, fees payable to TFM and other potential uses of cash. During the first quarter of 2016, TFG secured a US$75m revolving credit facility to give additional flexibility, in particular to exploit opportunistic investments.

TFG pays TFM management fees equal to 1.5% per annum of TFG's net assets. On a quarterly basis, TFG also pays TFM an incentive fee equal to 25% of the increase in NAV above a hurdle, calculated as the higher of the two prior quarter-end NAVs (adjusted for dividends and capital adjustments) plus a hurdle rate, equating to three-month US dollar Libor plus 2.65% pa (giving hurdle rates for Q1, Q2 and Q316 of 3.26%, 3.28% and 3.30%). If the hurdle is not met in any calculation period, the shortfall is not carried forward to future periods. Management and fee structures vary across peer companies, making a broad comparison difficult, but, for reference, we note that Carador Income Fund has a 1.5% pa management fee and a 13% performance fee, above a hurdle of Libor (subject to a 4% pa floor) plus 2%.

In addition to management and performance fees, TFG bears all direct investment-related expenses, including brokerage commissions, interest on borrowings, custodial fees and legal and consultant fees as well as administration costs, which were largely offset by fee income in 2015. TFG's ongoing charge for 2015 was 1.75% of average net assets (5.12% including performance fees).

Dividend policy and record

TFG pursues a progressive dividend policy with a target payout ratio of 30-50% of normalised earnings (incorporating both investment income and capital gains), based on its long-term target ROE of 10-15%. The board declares dividend payments, subject to the approval of TFG's voting shareholders. The level of dividend declared reflects a variety of considerations, including:

- the expected short- and medium-term sustainability of TFG's cash generation capacity,
- TFG's recent and anticipated performance,
- the current and anticipated operating and economic environment, and
- other potential uses of cash ranging from preservation of TFG's investments and financial position to other investment opportunities.

TFG currently pays scrip dividends through an optional dividend reinvestment programme.

TFG declared a Q415 dividend of US$0.1650 per share, a 1.5% increase on the US$0.1625 paid for Q2 and Q315, which followed the US$0.1575 dividends paid for Q115 and Q414, continuing the progressive dividend policy that it has operated since re-basing the quarterly dividend in 2009. The

US$0.6475 total dividend for FY15 represented a 4.9% increase over FY14 and equated to a 6.5% yield on the US$9.91 end-2015 share price. Following a similar pattern to previous years, the Q116 dividend was held at US$0.1650 and the Q216 dividend was increased to US$0.1675 per share.

Peer group comparison

Exhibit 16 shows a comparison of TFG with funds classified within the AIC Flexible Investment sector, comprising companies with a diverse range of investment strategies, and selected other investment companies. Blackstone/GSO Loan Financing, Carador Income Fund and Fair Oaks Income Fund are all AIC Sector Specialist: Debt funds that focus on CLO securities, which represent TFG's largest portfolio exposure, although no longer its primary focus.

TFG's NAV total return has substantially outperformed the Flexible Investment sector average over one, three and five years, and ranks at the top of the sector in all three periods. TFG's NAV total return also compares favourably with the other selected peers over the periods shown. In spite of TFG's strong performance record, its share price discount to NAV is the widest across both peer groups, suggesting that factors such as perceived lack of share liquidity may be having a significant influence. TFG's ongoing charge is at the top end of the Flexible Investment sector, but similar to Carador Income Fund, among the selected peers. TFG is ungeared, similar to the majority of peers, and holds a structural cash position. TFG's 6.1% dividend yield ranks as the highest within the Flexible Investment peer group but lower than the selected peers investing primarily in CLOs.

Exhibit 16: Flexible investment and alternative assets peer group comparison as at 8 September 2016

% unless stated	Market Cap US$m	NAV TR 1 Year	NAV TR 3 Year	NAV TR 5 Year	Discount (ex-par)	Ongoing Charge	Perf. fee	Net Gearing	Dividend yield (%)
Tetragon Financial	1,032.0	18.5	47.2	105.4	(46.2)	1.75	Yes	100	6.1
BACIT	647.8	(14.6)	(1.1)		3.1	1.27	No	100	1.8
BlackRock Income Strategies	401.8	(19.2)	(11.2)	(1.7)	(13.0)	0.69	No	116	5.8
Capital Gearing	181.2	(7.3)	(0.1)	4.1	1.5	1.04	No	100	0.6
Henderson Alternative Strategies	140.5	(11.3)	(11.7)	(32.6)	(16.9)	0.97	Yes	100	1.3
Invesco Perp Select Balanced	12.3	(7.7)	4.1		(1.6)	1.20	No	100	0.0
Miton Global Opportunities	63.1	(7.2)	5.2	3.2	(8.1)	1.16	No	103	0.0
New Star Investment Trust	85.6	0.9	8.3	1.2	(32.3)	0.93	Yes	100	0.3
Personal Assets	957.7	(1.2)	6.4	6.9	0.8	0.95	No	100	1.4
RIT Capital Partners	3,611.6	(8.1)	12.7	18.4	4.6	1.34	Yes	108	0.0
Ruffer Investment Company	471.5	(11.9)	(5.8)	(0.9)	(0.1)	1.13	No	100	1.5
Flexible Investment sector average	691.4	(6.3)	4.9	11.6	(9.8)	1.13		102	1.7
TFG's rank in sector	2	1	1	1	11	1		4	1
Other selected peers									
Blackstone/GSO Loan Financing	354.1	8.0			(2.4)		No	100	10.3
Carador Income Fund	402.0	(6.3)	7.2	68.4	3.7	1.86	Yes	100	12.2
Fair Oaks Income Fund	318.3	7.3			7.1	0.60	No	100	10.0
Selected peer average	358.1	3.0	7.2	68.4	2.8	1.23		100	10.8

Source: Morningstar, Edison Investment Research. Note: Performance data to end-July 2016. TR = total return in US$ terms. Net gearing is total assets less cash and equivalents as a percentage of net assets.

The board

TFG's board comprises six directors, four of whom are independent. The non-independent directors are TFG co-founders Reade Griffith (appointed April 2007) and Paddy Dear (appointed August 2005) who have executive responsibilities. The independent directors are Rupert Dorey (appointed August 2005), Frederic Hervouet (appointed July 2014), David Jeffreys (appointed August 2005) and William Rogers (appointed June 2016), who all have significant experience in asset management and financial markets. After more than 10 years' board service, Byron Knief stepped down in June 2016. Each board member is elected annually by TFG's voting shareholders.

Reade Griffith is a principal of TFM, head of TFM's Investment & Risk Committee, a member of TFM's Executive Committee, CIO of Polygon's European event-driven equities strategy and a member of the Investment & Management Committee of TCIP and TCI II. He was previously a partner and senior managing director at multi-strategy hedge fund Citadel Investment Group, responsible for running the Global Event Driven arbitrage team in Tokyo, London and Chicago, subsequently founding and acting as CEO of Citadel's European office.

Paddy Dear is a principal of TFM, a member of TFM's Investment & Risk Committee, a member of TFM's Executive Committee, a member of the Investment & Management Committee of TCIP and TCI II, and co-Head of TFG Asset Management. He was previously managing director and global head of Hedge Fund Coverage at UBS Warburg Equities, responsible for the delivery of all products and services to hedge fund clients globally.

Rupert Dorey has over 30 years' experience in financial markets, including 17 years at Credit Suisse First Boston focusing on debt distribution, origination and trading, covering all types of debt from investment grade to high yield and distressed debt. He is a director of NB Global Floating Rate Income Fund and AAA Guernsey (AP Alternative Assets).

Frederic Hervouet has over 17 years' experience in financial markets and hedge funds, including multi-asset class investment and risk management, structured products and structured finance, working at BNP Paribas, Diapason Commodities Management, Systeia Capital Management and BAREP Asset Management.

A qualified chartered accountant, David Jeffreys spent 15 years at Scandinavian private equity group EQT and 11 years as managing director of Abacus Fund Managers, involved with private client trust arrangements, corporate administration, pension schemes and fund administration.

William Rogers retired from law firm Cravath, Swaine & Moore in December 2015 after 36 years, having served as corporate department managing partner from 1998 to 2001. Counting TFG among his clients, he regularly advised on international securities offerings, corporate governance and SEC compliance matters, mergers and acquisitions, and derivative financial products.

Appendix: Collateralised loan obligations (CLOs)

Collateralised loan obligations (CLOs) invest in a pool of broadly syndicated senior secured loans, covering a wide range of issuers and industries. The portfolio of loans is selected and managed by a collateral manager, who can actively buy and sell loans based on their perceived attractiveness. CLOs finance this pool of loans with a capital structure consisting of debt and equity. CLO returns are primarily driven by the difference between the cost of debt and the yield generated by the pool of loans, net of gains or losses on the portfolio. CLOs typically make attractive investments when loan yields are high relative to CLO debt costs and also when loan defaults are low and projected to stay low. CLO issuance is most likely to occur when the interest rate spread between assets and liabilities generates an attractive return to equity holders.

A key strength of the CLO structure is that the debt is committed for the life of the transaction. CLO debt covenants are cash flow based and therefore not directly affected by fluctuations in the market value of the underlying loans. Instead, covenants are dependent on whether the loan portfolio assets are meeting their payment obligations. If more than a predetermined threshold level of loans are not servicing payments, then cash that would have been distributed to the CLO equity holders is retained to provide enhanced collateral to the CLO debt holders. The CLO structure is such that, in the majority of situations, debt holders cannot oblige a CLO to sell assets.

In contrast to mortgage collateralised debt obligations (CDOs), which sustained high default rates and low recoveries, CLOs performed relatively well during the 2008 financial crisis. Due to additional purchased collateral taking the form of leveraged loans trading at a discount, CLOs were ultimately supported by more assets than at origination at a lower average cost. Consequently, as the market recovered and loan defaults declined, CLOs benefited from increased income, while liability costs remained unchanged, which translated into higher cash flows to CLO equity holders.

In general, loans in a CLO portfolio pay Libor-based coupons and the debt issued by a CLO pays interest at rates also based on Libor. As asset yields and debt costs both rise and fall with interest rates, the CLO structure is naturally hedged. Most new issue loans have a Libor floor at above the current rate. This means that as Libor rates increase, the CLO's debt costs will increase, but the asset yields will not increase until Libor rises above the floor level. Alternatively, if Libor rates rise at a slower rate than projected, CLO equity will benefit from the wider than anticipated spread between the asset yield and the CLOs debt costs while the Libor floor remains in effect.

Market prices for individual CLO equity positions are derived by discounting projected cash flows (TFG uses discount rates of 11.0%, 12.0% and 13.0% for its US 2.0, US 1.0 and European CLOs), with no widely-used pricing benchmark for either CLO debt or equity. Key coverage tests for a CLO are overcollateralisation (OC), interest coverage (IC) and interest diversion. OC tests compare the par values of a CLO's assets and its debt. IC tests compare the CLO's interest receivable with its debt interest cost. The interest diversion test is an 'early warning' OC test; if failed, a portion of the interest payable to equity holders is instead reinvested in the CLO and used to buy additional assets. If an OC or IC test is failed, interest proceeds are used to repay the CLO's debt. At issuance, the tightest coverage tests typically have a 3-4% cushion from their required threshold.

CLO equity holders control the right to redeem CLO notes after a non-call period (typically one to three years for CLOs issued since 2010 and three to five years for 2003-07 vintage CLOs), usually subject to a majority or two-thirds voting in favour. Equity holders may choose to exercise this call option if either the expected forward return no longer offers adequate compensation for the assessed default risk or if market rates make it possible to refinance the debt at lower cost. Once equity holders satisfy a CLO's trustee they have sufficient collateral to cover all liabilities and expenses, it is relatively easy to call the deal, with the process typically taking around three months to complete. Although a call may make economic sense for equity holders, the CLO manager is incentivised to leave the deal outstanding and continue to earn fees and, if a CLO has a dispersed group of equity holders, it may be a challenge to aggregate a majority stake to call the deal.