Round Hill Music Royalty Fund

Initiation of coverage

Music and finance in harmony

Investment trusts
Special situations – music royalties

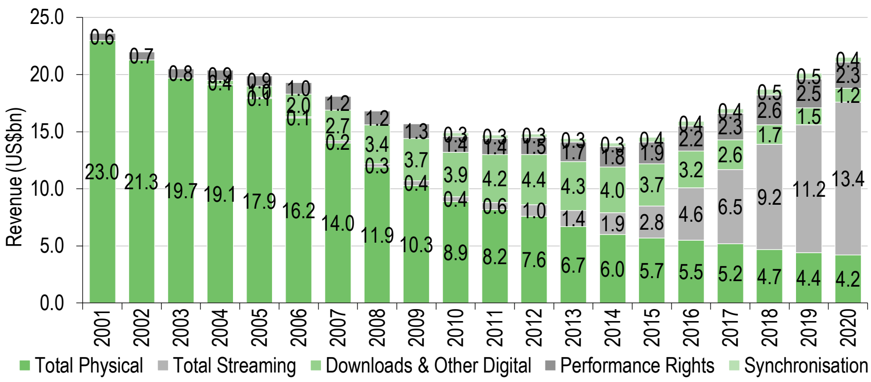
17 August 2021

Round Hill Music Royalty Fund (RHMRF) was launched in November 2020. Its fund manager, Round Hill Music LP, established in 2010, manages over $900m (at end June 2021) and is one of the largest global music asset owners, consistently a top 10 Billboard Top Publisher. RHMRF benefits from Round Hill's industry expertise and fully integrated business owning and exploiting music copyright assets. It focuses on mature catalogues (90% of its songs are over 10 years old) and high growth-potential master rights (c 23% of portfolio at June 2021). We believe RHMRF's assets to be high quality, with strong potential to provide reliable and growing revenues given the momentum in streaming and potential of new channels.

Price	**$1.06**
Market cap	**$350.9m**
NAV*	**$344.7m**

NAV*		$1.05
Premium to NAV*		1.2%
*As at 31 March 2021.		
Yield (prospective)		4.5%
Ordinary shares in issue		330.1m
Code/ISIN		RHM/GG00BMXNVC81
Primary exchange		LSE
AIC sector		Specialist – royalties
52-week high/low	$1.08	$1.00
NAV* high/low	$1.05	$0.98
*NAV as reported in the accounts on 31 March 2021.		
Net gearing**		109%
**As at 30 June 2021, defined as total assets) less cash to NAV*.		

Global recorded music revenues by segment 2020



Source: IFPI

Fund objective

Round Hill Music Royalty Fund's investment objective is to provide investors with an attractive level of regular and growing income and capital returns from investment primarily in high quality music intellectual property. To achieve this objective, it seeks to invest in a songwriter's copyright interest in a musical composition or song, together with the rights in the recording of these (known as the master recording rights), along with all other rights and assets considered relevant by the manager.

Bull points

- Strong mix of professional music and finance experience in core investment team.
- Relatively high predictability of returns.
- Prospect of more favourable regulation.

Bear points

- Competitive market for assets.
- Risk of overpaying for assets.
- Regulatory changes may or may not be beneficial.

Why invest in music royalties?

The growth of streaming has fundamentally shifted music industry economics, reducing piracy and increasing the value of the underlying asset: the music. A new group of companies has emerged to curate these assets, alongside the major publishers. They are driving revenues by encouraging song plays and usage in other applications, as well as improving the efficiency of royalty payment collection. Artists and songwriters are realising the value of their output and there is an active market in music portfolios. Regulators are siding with songwriters over increasing their revenue share versus both streamers and music publishers, indicating further possible valuation uplifts that should benefit publishing and master rights owners.

The analyst's view

In our view, RHMRF has compiled a strong set of assets through its purchases of the Round Hill Fund One assets and the outstanding minority interest of the Carlin portfolio. We regard the prices paid as appropriate for the underlying asset quality, which is mature and well diversified by genre. RHMRF's revenues are set for strong growth, driven by the popularity of streaming and newer formats such as social media, gaming and fitness. The prospect of regulatory changes that are considerably more favourable to songwriters enhance the outlook further. The manager Round Hill (RHM LP) has generated a historical internal rate of return of over 17% (over the past 10 years) on its three private funds.

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Edison profile page

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Fund profile: 'High quality' music royalties specialist

RHMRF listed on the London Stock Exchange on 13 November 2020, with the IPO raising $276.4m. It is the second UK-listed closed-end fund investing in music royalties (following Hipgnosis Song, SONG, listed in July 2018). Its net asset value (NAV) is currently $344.7m (as reported in the accounts on 31 March 2021 and $323.5m based on $0.98 economic NAV per share at launch) and the market capitalisation is £258.3m ($350.9m). A secondary fund-raise in December 2020 raised $46.1m net (46.1m shares at $1.01) and the fund has recently (July 2021) raised a further $86.5m in a 'C' share issue. Both raises were within its placing programme. Exhibit 1 below summarises RHMRF's capital raises to date.

Exhibit 1: RHMRF's capital raises and monies invested to 31 July 2021

Date	13-Nov-20	16-Dec-20	2-Jun-21	16-Jul-21	31-Jul-21	31-Jul-21	31-Jul-21
Event	IPO	Placing	Share issuance	C share placing	Total new Ord shares	Total new C shares	Total voting rights
Number of shares (m)	282	46.1	2	86.5	330.1	86.5	416.6
Price per share ($)	0.98	1.01	1.00	1.00	N/A	N/A	N/A
Total raised ($m)	276.36	46.561	2	86.5	411.4	N/A	N/A
Capital invested ($m)	N/A	N/A	N/A	N/A	342	N/A	N/A

Source: RHM, Edison Investment Research

The company seeks to invest in music royalties with a proven track record, with wide audience appeal.

In February 2021, RHMRF completed the acquisition of its first investment, which consisted of the assets of Round Hill Fund One, less the 29.14% minority investment in the RH Carlin portfolio. These assets were bought for $282m, the amount of the IPO proceeds (86% of the IPO proceeds plus December 2020 raise). The Carlin minority was subsequently purchased shortly after, in April 2021. The majority ownership (70.86%) of Carlin rests with Round Hill Fund Two and a Carlin co-investment vehicle (see the Investment manager section on page 3). At the time of the second acquisition, RHMRF announced that it had entered into a revolving credit facility (RCF) with Truist, allowing it to draw up to 25% of the fund's economic value, which part funded the Carlin purchase.

- The first investment consists of 38 catalogues, containing over 18k songs, purchased at 16.3x net publisher's share (NPS). This catalogue had generated revenues of over $83m prior to its purchase.
- The second investment (the Carlin minority investment) consists of over 100k songs in one catalogue, bought at 16.2x NPS.

Further details of the investments are given below.

RHMRF targets a total return (TR) to investors of 9–11% over the medium term, after fees and expenses. The company also targets a 4.5 cents per share annualised dividend payment, payable quarterly.

The fund manager: Round Hill Music Royalty Fund (RHMRF)

The manager’s view: Consistent royalties income stream

RHMRF believes it is well positioned to take advantage of the strong current growth in the music industry. It envisages the market for publishing and recorded music doubling within 10 years, mostly due to the growth of streaming (a view that coincides with independent sources). It points to several trends within what it calls ‘a golden era of deal flow’. During 2021, the investment team expects continued growth in the number of paying digital music subscribers as providers extend their reach in established territories and grow strongly in emerging markets. It believes Spotify’s move to increase the price of its premium service in over 40 countries is likely to result in increased publishing revenues, which will flow through to RHMRF’s revenues. There is also increased monetisation of music content from new formats such as short form video, connected fitness and gaming.

The COVID-19 pandemic has benefited streaming but affected performance royalties. The demographic profile for streaming subscribers has skewed towards the older age group, which sits well with the manager’s approach to catalogue acquisition.

Performance royalties in FY20 and into FY21 have been severely affected by lockdowns, with management estimating the likely current year impact as a decrease of 20%. With streaming and mechanical royalties (for definitions, see below) set to be strong, it anticipates that music publishing revenues overall will be up around 5% globally.

RHMRF also has a relatively high proportion of Master rights (defined below), which contribute c 23% of royalty income. This gives a degree of protection should the distribution of royalty revenues change between the various participants in the value chain.

The manager considers that the current set of circumstances provides an attractive investment environment, with the inability to tour causing artists to lose a high proportion of their income and forcing them to look to other ways to generate an income. Many older artists are also looking to optimise their tax and inheritance positions through the sale of their works.

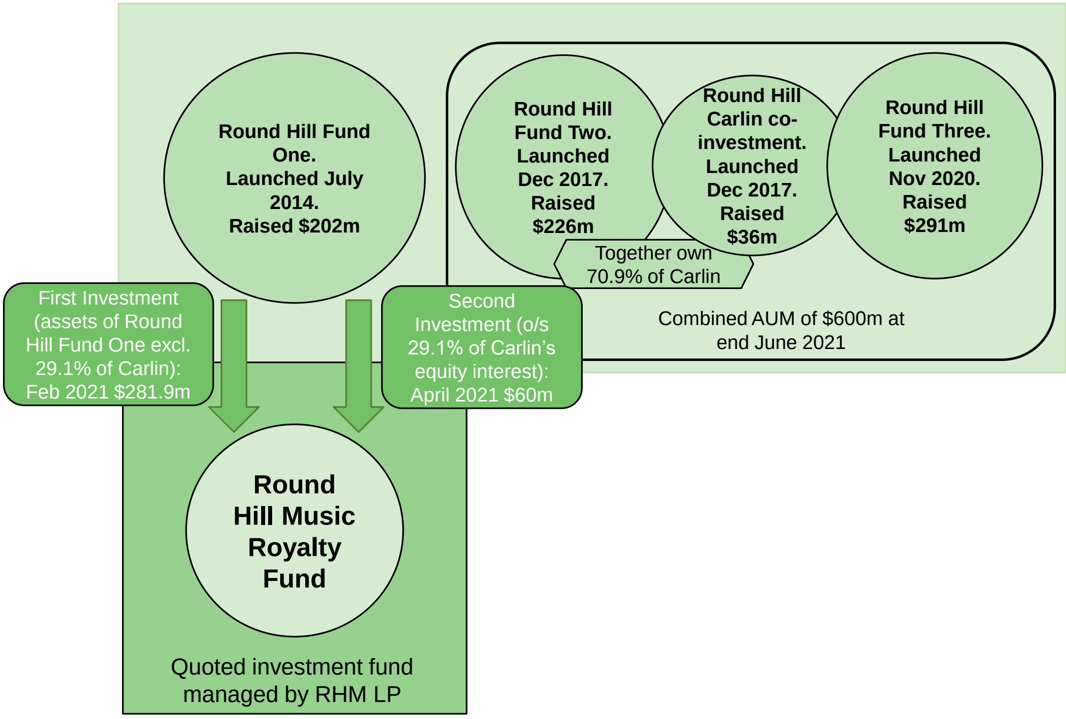
Investment manager

RHMRF's investment manager is Round Hill Music LP (RHM LP). Founded in 2010 by CEO Josh Gruss, it is dedicated to acquiring and managing music copyright properties with in-house, full-service copyright registration and royalty collection, licensing administration and synchronisation operations. Since its inception, RHM LP has completed over 130 catalogue investments to date, held within three funds, as illustrated below. The first of these has now been acquired by RHMRF.

Most of RHMRF’s assets are intangible and primarily consist of music intellectual property. The current portfolios managed by RHM LP contain over 130,000 songs, diversified across artist, genre, decade and royalty type. It has a strong acquisition track record and has completed 65 transactions in the last year for Round Hill Fund Three. The weighted average multiple for these deals was 14.3x last three years’ NPS.

The investment manager’s mission statement is: RHM LP ‘is committed to building a catalogue of great songs, of being the best and most innovative publisher for word-class songwriters, composers, music royalty investors and management talent, and the first-choice music source for creators in all media.’

Exhibit 2: Structure of investment manager and funds



Source: Edison Investment Research

The team

RHM LP's investment management team is led by an experienced management team of six managers. This team is distinguished by its mix of professional experience within the music and finance industries, with over 150 years of combined music and institutional investment experience. Josh Gruss is founder and CEO of RHM LP. He is an experienced international financier and music professional with over 24 years in those industries, educated in the US and UK. Neil Gillis, who is based in the US, joined RHM LP in 2010, is president and has over 37 years' experience in the music industry, specifically in music publishing. Steve Clark joined RHM LP as COO in 2020 with over 32 years' industry experience, including senior operating management roles at Warner Chappell Music, and is based in the UK. There are two CFOs. Amanda Siconolfi (who joined RHM LP in 2015; CFO since 2020) is focused on finance and investments, while Shannon Farley (who joined RHM LP in 2018 with over 10 years of fund operational experience at Blackstones's real estate funds; CFO since 2020) oversees the funds and operational side of the business. Erich Carey is the internal legal adviser. He joined RHM LP in 2019, with 11 years of legal experience in the music industry. Carey is also RHM LP's head of business affairs and overlooks the investment process from start to finish.

RHM LP's headquarters are in New York, with additional offices in Nashville, Los Angeles and London. Steve Clark is based in London, while the rest of the core team are in New York. The managers are supported by a team of over 55 professionals across the four offices globally, and most employees are based in Nashville, the hub of the music royalty world. Their expertise and capabilities include a multi-territory copyright and royalty team, licensing, creative sync and master recording rights management. Mark Brown is the general manager in Nashville with over 35 years in the business and is an expert on the country music market. Marissa Baldi is the head of sync and previously worked at Universal Music Publishing. Most of the Zync crew is based in Los Angeles, an important hub for film and tv licensing.

Music copyright: A labyrinthine process

RHM LP's business model is based on the foundation of the value inherent in music **copyright**. This is realised in the payment of **royalties**, which are defined as legally binding payments made for the ongoing use of assets. These assets include copyrighted works, such as music.

Copyright arises at the moment a composition is created and fixed, be that documented or recorded. Ownership of the copyright entitles the owner the rights to publish the music by:

- copying the music,
- issuing, lending or renting copies to the public,
- performing, showing or playing the music in public, and
- communicating the music to the public, for example by broadcasting it via various media.

Copyright typically lasts until 70 years after the death of the last living songwriter, under the internationally recognised Berne Convention. This is a key factor underlying the growth of copyright ownership as an asset class, together with the comparative predictability of revenues once songs have reached a certain maturity.

There are two specific types of music copyright: **publishing rights** and **master rights**. Round Hill has interests in both.

The various types of royalties are illustrated below.

Exhibit 3: Types of music royalty

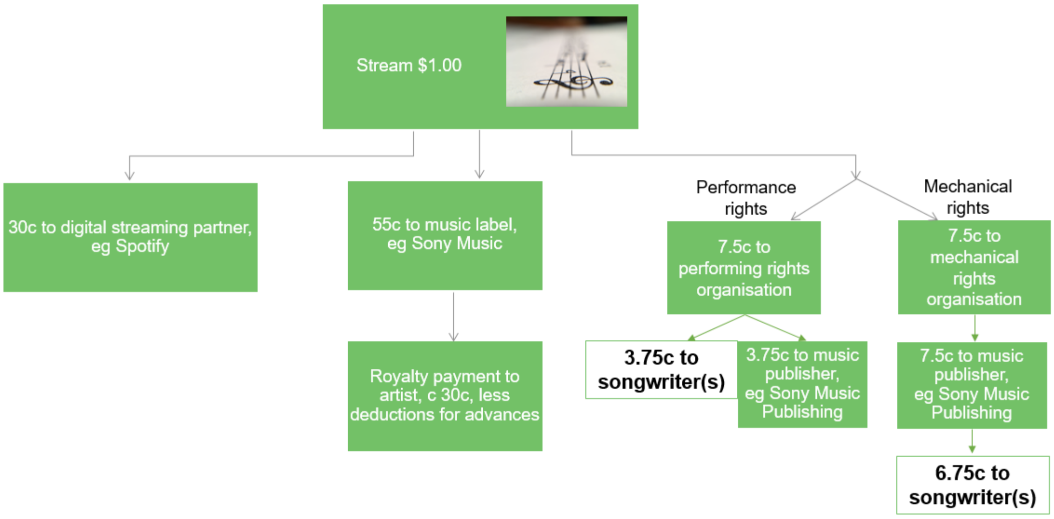
Type of royalty	Use case	Typical licensor	Method of collection
Performance	Public broadcast in a commercial environment	Live concerts, Netflix, YouTube, gyms, restaurants etc	Via PRO
Neighbouring rights (aka Masters' royalties)	As per performance but relating to the particular recording	As above	Via PRO
Synchronisation licensing fees (Sync royalties)	Where music is used in conjunction with visual imagery	TV/ film content, advertisements, games, Peloton etc	1:1 deal. Needs publishing and master use licensing
Mechanical	Physical media and digital downloads	CDs, vinyl, Blu-Ray plus Apple, Amazon etc	Contractual
Digital performance	Internet/satellite radio, webcast	Deezer, Sirius XM, Google Play Music	Sound Exchange in US (pays 45% to feature artists, 5% to non-featured and 50% to Master rights holders)
Digital/streaming	Streamed on digital platform	Spotify, Apple Music, Amazon music, Deezer	See below
Other	Sheet music, cards, clothes, toys, theatre etc	Various	

Source: Edison Investment Research. Note: PRO = performing rights organisation.

Management groups such as RHM LP primarily focus on the publishing rights but may have some interests in the master rights in some instances. Publishing rights belong to the owner of the composition, which would normally be the songwriter(s) and which may then be shared with a publisher. The master rights relate to the particular recording of the song, so a cover version would generate a different master right to the original recording, despite it being the same song. These rights belong to the artist(s) and to the record label. The master rights are generally equated with the value accorded to the recorded music industry, described below.

Royalties are the monies paid to copyright holders to license the use of the intellectual property, in this case, the song. In cases where the royalty is collected by a performing rights organisation (PRO), the process is comparatively straightforward. This is not the case for streaming, which obviously post-dates the regulatory framework, which has had to bend to adapt. An outline of how a royalty payment from a stream may reach the rightsholder is illustrated below, although this is a pared-back version.

Exhibit 4: Illustrative flow of funds from a stream



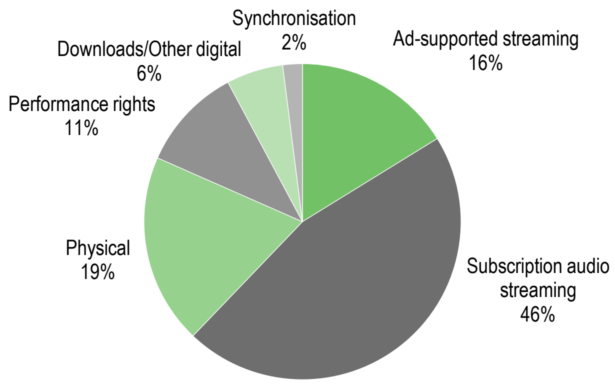
Source: IFPI, DCMS Report on the Economics of Music Streaming, Edison Investment Research

The music industry is undergoing significant changes

The recorded music industry has seen six years of consecutive growth driven by the widespread adoption of paid subscription streaming services, with global revenues growing at CAGR of c 9% (FY14–20) to reach $21.6bn in 2020. This followed a 15-year period of decline, where revenues went from a peak of $29bn in 1999 to a low of $14bn in 2014 (IFPI/Statista). This decline was fuelled by the interruption to the CD era by MP3s and file sharing, which fostered a culture of piracy. (see chart on page 1).

In tandem, global music publishing revenues grew by a CAGR of 7% between 2015 and 2019, reaching $5.6bn (2014: $4.2bn). Alongside streaming, both publishing and recorded music should continue to benefit from increased smartphone penetration, the increasing prevalence of smart speakers, growth of social media and new technologies, which have made music more accessible than ever.

Exhibit 5: Music industry global revenues by type FY20



Source: IFPI. Note: All statements in this document attributable to IFPI represent Edison Investment Research's interpretation of data, research opinion or viewpoints published as part of the IFPI Global Music Report in March 2021, and have not been reviewed by IFPI. Each IFPI publication speaks as of its original publication date (and not as of the date of this document).

The current battle for influence

The very low average sums accruing to originators from the streaming platforms have led to an increasingly loud debate over the economic influence of songwriters, without whom there would be no music to stream. With a handful of powerful platforms and a handful of powerful music publishers, it was relatively easy to side-line the originators of the content. However, some high-profile voices cut through and drew the attention of regulators, as well as a proportion of the fans who have been campaigning for a more equitable distribution. The onset of the pandemic and consequent suspension of live gigs and tours (and sale of merchandise) further highlighted just how little songwriters were earning from the digital streaming platforms.

In the US, a body called the Union of Musicians and Allied Workers was set up to campaign to challenge the pro-rata system of royalty distribution used by Spotify, which favours current mass appeal artists, exaggerated further by algorithmically curated playlists. Under the pro-rata system, subscriptions are pooled into a single pot, then allocated according to the proportion of streams. One alternative model is a user-centric model that apportions payments according to what individual users consume.

There is a further potential tension between artists and their labels, with the proportion of royalties paid across to artists and songwriters varying by their contracts, albeit that the percentage has been rising over the years. Some labels do not pay across royalties until they have recouped their costs, mostly the advances extended to artists to attract them to the label but also including marketing costs. These can be so substantial that the artists may not ever earn anything from their work.

These factors are all being examined and updated. In the United States, the US Copyright Office has brought forward The Music Modernization Act, which pulls together the requirements for digital music providers to pay licence fees and distribute royalties via an online portal, which brings more visibility and consistency into the process. In the UK, a parliamentary committee has been examining the industry ecosystem. Its key findings and possible repercussions are examined below. While any changes to the UK system would not directly affect US royalty payments, they would be closely observed and may be used to exert pressure towards similar objectives.

Findings of the UK DCMS Committee report on the economics of music streaming

A cross-party parliamentary committee of the Department of Culture, Media and Sport has taken evidence from over 80 interested parties (including the digital streaming platforms, labels and artists) over recent months. It has now published its report and recommendations, which could have a dramatic impact on the ecosystem if implemented in full. This is important globally as artists who achieve a more equitable framework in the UK are going to demand better recompense for their output wherever it is consumed. In this context, it is worth noting that the UK music sector is the third largest globally after the US and Japan.

Its key findings are that royalty rates paid to content creators are poor, there are disadvantageous splits between publishing rights and master rights and that, generally, the ecosystem is inconsistent and not fit for purpose. The system as it stands particularly favours the small cohort of powerful music labels (Universal Music Group, Warner Music and Sony Music), which may also be vertically integrated as music publishers. The report is also critical of those platforms (particularly YouTube) with user-generated content that allows them ‘safe harbour’ from liability for copyright infringement (unless they have specific knowledge). Within the EU, this side-step will shortly be ruled out by the adoption of the Directive on Copyright in the Digital Single Market.

Key recommendations of the report include:

- Artists/songwriters should have the right to equitable digital music remuneration. In this context, 'equitable' means 50:50 between the artist and the label.
- Artists/songwriters should be able to recapture the rights to their work after a period of time. The suggestion here is that the period should be set at 20 years, considerably shorter than the 35 years in the US. This is unlikely to be popular with the major labels, which will very probably be pointing out their upfront investments.
- Artists/songwriters should have the right to adjust their contracts if a work is more successful than originally anticipated, for example if it is used in a high-profile advertisement. Sony Music have already adopted this course and the committee strongly recommends that the others follow.
- The committee suggests that the Competition and Markets Authority looks into the power wielded by the music majors. However, they cannot be obliged to act and any such investigation would take time to scope and then research, before any consequent actions are required.
- The committee recommends that conditions be normalised between the streamers and other routes to market, particularly in terms of the safe harbour rules relied on by YouTube. It also recommends that action is taken to avoid algorithms and playlist curation being 'played' for gain (such as lower royalty for higher prominence offsets).
- The committee recommends that the industry steps up its ability to tag works with metadata (ISRCs to apply to the particular recording and ISWCs to apply to the song itself). Efforts to pull this together previously have failed due to lack of incentives for the music labels to comply. The committee is also disparaging of the common use of NDAs in the music industry, which make it difficult for an artist to audit what income they are due from the streamers. One of the key 'wins' for the likes of Round Hill and Hipgnosis has been in the matching of incomplete and incorrect data to claim back unpaid royalties.

For Round Hill and other rights owners, we judge the tenor of the report to be favourable. If the recommendations are adopted, either through the Private Members Bill put forward by one of the committee, which is due for its second reading in the autumn, or through some other act of parliament, we believe that the value of the rights in the portfolio should be enhanced due to the increased share of revenues flowing back to songwriters.

Any limitation on the recapture of rights is not made clear by the report – whether recapture is for content created after the first signing of an artist to a label or if the concept is to allow rights to revert to the creator every 20 years. We suspect the intention is for the former and that the sale of rights later in an artist's career, such as to Round Hill or a similar purchaser, would not be for a fixed period. If implemented, this should mean that there will be more rights available to buy on a more regular basis and therefore a more active market in the longer term.

Uncertainty and opportunities spurring corporate activity

As described above, the combination of circumstances has prompted an upturn in the number of catalogues changing hands. However, the whole of the music industry is undergoing a rebalancing. Publishing is dominated by a handful of major, global concerns, namely Sony Music, Kobalt Music Services, Warner Music, Universal Music Group and BMG Rights Management.

Below we pick out some of the key industry transactions that have taken place so far in 2021 (it is not exhaustive). It is worth noting the number of deals involving special purpose acquisition companies (SPACs), including I2PO, the latest to join the roster, which has raised more than its €250m target.

Exhibit 6: Notable music industry transactions 2021 to date

Date	Company	Detail
29/7/21	Reservoir	Floated on NASDAQ as SPAC merger. Owns >130k copyrights and 36k master rights
19/7/21	Universal Music	Pershing Square Tontine pulls out of 10% purchase in favour of Pershing Square Holdings
16/7/21	I2PO	European SPAC focused on entertainment & leisure (with reported music focus) raised €275m
24/06/21	Universal Music	Licensing deal with Snap.
22/06/21	Sony Music	Buys majority stake in Alamo Records for reported $125–200m
21/06/21	Songtradr	Raised $50m in an oversubscribed series D funding round. Has raised > $100m, valued at $300m+
20/06/21	Universal Music	US SPAC Pershing Square Tontine Holdings bought 10% for c $4bn, an implied valuation of $40bn
17/06/21	Warner Music	Acquired David Guetta's recording catalogue for over $100m
16/06/21	Hipgnosis Songs Fund	Follow-on raise of $210m
11/06/21	Primary Wave	Oak Tree Capital injects $375m for minority stake
01/06/21	Believe	Oversubscribed 10% IPO raising €330m, valuing company at €1.9bn
03/05/21	Warner Music	Acquired majority stake in Wave, a virtual concert platform, price undisclosed
27/04/21	Songtradr	Acquired film, tv and gaming music platform Tunefind, price undisclosed
20/04/21	Songtradr	Acquired pretzel, providing music for twitch and YouTube live streamers
14/04/21	Reservoir	Listing on Nasdaq via SPAC merger with a $788m valuation, expected to close Q321
02/04/21	HYBE/ Big Hit Entertainment	Acquired Ithaca Holdings (Scooter Braun's company) for a reported $1bn
01/04/21	Universal Music	Agreement for new five-year $3.5bn financing line. Goldman Sachs values it at $53bn ahead of IPO, expected by end 2021
01/04/21	Sony Music	Acquired Som Livre, Brazil, for $255m from Globo group
24/03/21	BMG/KKR	Companies agree to jointly buy music copyrights
22/03/21	Warner Music/Tencent Music Entertainment	Launched Chinese JV
02/03/21	Netease/Sony Music	Joint $15m Series B investment round for live-streaming platform Maestro
24/02/21	Spotify USA Inc	Convertible raise of $1,300m
05/02/21	Hipgnosis Songs Fund Ltd	Follow-on raise of $103m
02/02/21	Music Acquisition Corp	IPO raising $200m
01/02/21	Sony Music	Paid Kobalt $430m to acquire AWAL and Kobalt Neighbouring Rights
29/01/21	Primary Wave	Acquires Sun Records for reported $30m

Source: Edison Investment Research

Strategy and investment process: In-house expertise

RHMRF's investment objective is dual:

- provide investors with an attractive level of regular and growing income, and
- deliver capital returns from investing in music intellectual property.

The company predominantly invests in small to medium-sized catalogues (typically 100–1,000 copyrights), diversified by artist, genre, decade and royalty type, usually purchased directly from songwriters or their estates. RHMRF (and the investment manager RHM LP) typically focuses on catalogues that are in the $1–50m range, and hence are often overlooked by major publishers, who generally look to purchase larger catalogues. It uses strict acquisition criteria to select catalogues perceived to be of high value by the investment team, that may have been under-exploited by their previous administrators.

RHM LP focuses predominantly on classic, older copyrights with enduring appeal and which experience consistent usage, particularly in the pop and rock genres. Such compositions have generally reached a steady state and are not subject to the natural decline in earnings and value that typically occurs within the initial 10 years of a composition's life. They often also have the longest licence, typically owned for life of copyright. RHMRF has c 95% of its portfolio invested in catalogues of songs over 10 years old (see Portfolio section).

The majority of the returns from the company's investments are derived from the royalty streams. In addition, RHM LP seeks to enhance returns through improved royalty collection, pro-active licensing activity and increased usage and song exposure, using its own internal synchronisation team, Zync, acquired in 2017. The investment manager leverages current software and technology to handle royalty accounting and marketing to prioritise its resources on the highest risk-adjusted return activities.

RHM LP has its own recording studios in Nashvillle (called Sienna Studios). The manager also has their own record labels (Black Hill for rock, Triple Crown for ASlternative, Round Hill Records (soul, blues, jazz).

The company (RHMRF) may acquire copyrights for cash and/or shares. It may also acquire vehicles (or interests in such vehicles) that own catalogues as opposed to the catalogues themselves. It may also, subject to the approval of the board and shareholder approval, acquire copyrights and catalogues from RHM LP, parties related to the investment manager and funds managed by the investment manager, as outlined in the IPO prospectus.

Investment process

The investment team uses its broad network of longstanding relationships with songwriters, music entertainment lawyers, business managers, estate trustees and other prominent advisers to music catalogues to source transactions. RHM LP reviews approximately 75 to over 100 investment opportunities annually and expects only a subset of these to meet initial screening requirements, leading to further due diligence.

The acquisition criteria RHM LP looks for in a catalogue are:
1. well known iconic songs,
2. administration and licensing control,
3. long term ownership of rights,
4. contribution to catalogue diversity,
5. non-auction, proprietary deals; and
6. anticipated stability of cash flows.

RHM LP emphasises two main components of the due diligence process: financial due diligence; and legal due diligence. Two third parties (The Royalty Review Council and Selverne & Co.) are also used to supplement in-house due diligence.

RHM LP has developed and devotes extensive resource towards ensuring prompt and precise royalty collection. 19 administration staff work full-time on timely copyright registration and monitoring royalty collection, using Counterpoint, a specialist software system. There are 15 further full-time personnel dedicated to synchronisation licensing and six on artists and repertoire (A&R).

Operational enhancements programme

RHM LP has been implementing a series of operational initiatives over a rolling two-year plan to maximise collection of global royalties. This programme aims to turn separate databases and operational systems used by the company into a global single system, by January 2023. RHM LP's team is connected at a wider industry level, where it gives input and influence into general improvements in the music ecosystem, in order to improve usage matching and royalty flow.

RHM LP's music royalty valuations

RHM LP uses an independent valuer, Massarsky Consulting Inc., to value assets in the portfolio on a bi-annual basis. Massarsky is a leading specialist music consulting and valuation firm based in New York, whose clients include Sony Music, Universal Music and Warner Chappell, as well as a wide range of independent publishing companies, and Hipgnosis Songs Fund. It applies a conventional discounted cash flow methodology for musical compositions' valuations, discounting future earnings projections from a composition over a period of time (typically 20+ years).

Valuations are typically cross-referenced to transaction multiples based on NPS for publishing rights. NPS is calculated as gross income (the amount of royalties received by a music publisher) less direct costs, including royalties due to writers and performers, and catalogue administration.

Valuations and the associated multiples may be driven by a number of subjective factors, including:

- the popularity or reputation of an artist,
- the genre of the music, and
- the era of issuance (industry term is 'vintage') of the catalogue (eg 70s, 80s).

Older catalogues typically attract higher multiples as they comprise songs that have stood the test of time, tend to exhibit lower earnings volatility and are therefore deemed lower risk. These songs are often favoured for synchronisation, as they tend to have greater traction across demographics.

Newer catalogues are more difficult to value as future earnings are assumed to reduce over time. A song's popularity generally peaks in the first one to two years after release, decreasing over the following three to eight years. The pattern of revenue decay will naturally vary by song.

Business model

Active management is key to RHMRF's (and RHM LP's) business models. Most of the asset management is carried out in-house by RHM LP's publishing administration team of c 55 professionals (see above). The investment manager aims to maximise the value of its assets (predominantly catalogues) by

- active collection of royalties through efficient internal processes,
- licensing activity and song placement, and
- re-packaging and re-issuing master recordings.

RHM LP considers the risk of overpaying for a catalogue as its top business risk.

According to RHM LP, active management is often not reflected in underlying multiples. It regards valuations of 16–20x NPS for high-quality, iconic, blue-chip, stabilised catalogues as attractive.

RHMRF's pre-IPO prospectus (issued in Q420) outlines that between 2008 and 2014, catalogue valuations were typically 8–10x NPS. Since that period, valuations have risen to 9–15x NPS for new catalogues (with the most prestigious stabilised catalogues reaching 20x NPS). The Round Hill team cautions against using historical multiples to assess current deals or analyse valuations or implied yields, given the underlying shift in the market.

Despite the increased interest in the asset class in recent years, RHM LP believes that RHMRF can continue to acquire catalogues, particularly those of small to medium size, on attractive terms, due to its broad international network and deep relationships within the music publishing business,

The RHM LP team believes that master recordings present higher potential to enhance their asset value, due to their attractive low acquisitional multiples plus notable growth opportunities in digital.

NAV sensitivities and reporting

The key factors in music royalties' valuation models are:

- royalty revenues growth rates,
- the discount rate used in valuation,
- the initial acquisition valuation,
- the valuation time horizon, and
- the terminal value assumed.

RHMRF intends to publish NAVs twice per annum within its reporting. Under IFRS, the songs in the company's portfolio are classified as intangible assets under IAS 38. The catalogues are held at cost and amortised over their useful life (which is determined at acquisition), less any impairment. The directors also disclose the fair value of the portfolio of songs as determined by the independent valuer, Massarsky, using a discounted cash flow. This portfolio valuation forms the basis of what RHMRF calls the 'economic NAV' (Hipgnosis SONG calls this measure 'operative NAV'). We note that 'economic NAV' might differ from the portfolio value, as amortised cost has been used in the IFRS NAV in the accounts.

The company floated at $0.98 economic NAV per share.

Massarsky valued RHMRF's seed portfolio's First Investment (see the Portfolio section below) on 31 December 2020 at $303.7m, using an 8.5% discount rate. This was $21.8m (7.7%) more than the 30 June 2020 valuation, using a 9% discount rate. This would result in an increase in RHMRF's NAV of 6.6 cents/share to 104.6 cents/share (relative to 98.0 cents/share).

We note that Massarsky also valued the Hipgnosis portfolio at 30 September 2020 using an 8.5% rate (50bp down from its previous valuation six months earlier).

Portfolio

Acquisitions of the seed portfolio

On 2 February 2021 the board announced that it would acquire its pipeline assets in a two-stage process and completed the first step of the acquisition. The first investment completed on 1 February 2021 for a total cash consideration of $281.9m. This sum represented 86% of the gross proceeds raised in the RHMRF's IPO and the subsequent placing of 46.1m shares (at $1.01 per share) on 16 December 2020. This consideration equals the independent valuation of the assets acquired as at 30 June 2020.

Under the terms of the acquisition, the company is entitled to receive all income generated by the assets with effect from 1 January 2021, regardless of when the income was earned. The first investment includes iconic copyrights from artists including The Beatles, Marvin Gaye, Celine Dion, Rod Stewart, Phil Collins, James Brown, The Offspring, Kiss, Back Street Boys and Lady A. The first investment is extremely well diversified by genre and income type with a significant proportion of the copyrights originating from the 1960s to 1990s. Further details of the catalogues contained in the first investment are given below.

On 4 May 2021, the board announced the completion of the second step of its pipeline assets acquisition. RHM acquired a 29.14% share in RH Carlin Holdings LLC (Carlin, the second investment) that was previously owned by Round Hill Fund One. The balance is owned by Round Hill Fund Two and the Carlin co-investment vehicle. With this purchase, RHMRF successfully acquired all of the pipeline as identified in the company's October 2020 prospectus.

The consideration paid by the company in connection with the acquisition of the second investment reflects the underlying valuation of the copyrights owned by Carlin as of 30 June 2020. All income from the copyrights attributable to the company, in relation to its shareholding in Carlin, will accrue to the company from 1 April 2021.

Further pipeline assets

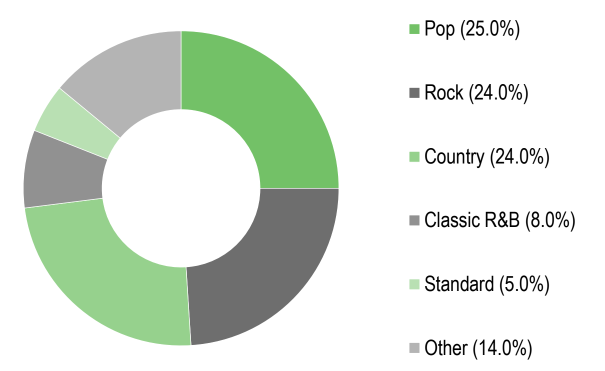
RHMRF announced on 24 June 2021 that RHM LP has identified, and is at an advanced stage of negotiation on, a pipeline of approximately $120m of investment opportunities. This pipeline includes music publishing, master recordings and neighbouring rights from various iconic artists, songwriters and producers. The rights involved span the 1960s to 1980s, and therefore fit well with the company's low-risk strategy of investment in classic songs. The music has global acclaim, with some originating from the UK, and songs are from the rock and pop genres. Some of the writers and artists involved have been recognised by the Grammy, Ivor Novello and Rock and Roll Hall of Fame committees.

RHMRF expects to deploy the net proceeds ($86.5m gross) of the July 2021 'C' Share Offer within three months of its closing. In addition, the company continues to build a pipeline, with an acquisition value of c $300m (at end-June 2021), substantially exceeding its recent equity raise. RHM LP has also seen significant deal flow emerge from within its existing catalogues (including the pipeline investments) and has a proprietary position on those deals.

Current portfolio positioning

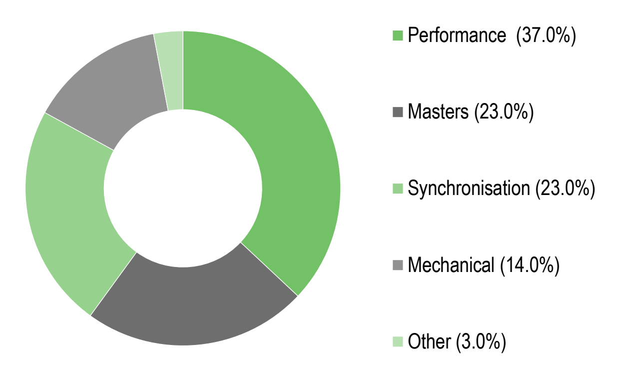
Following the acquisition of the seed portfolio in May 2021, RHMRF's pro-forma combined portfolio (first and second investments) has 39 catalogues with over 118,000 songs (at end-June 2021). Exhibits 7 and 8 illustrate the portfolio's split by genre and revenue type. Around three-quarters of the portfolio is fairly equally split between three genres: pop (25%), rock (24%) and country (24%). Notably, following the investment manager's 'high quality compositions' approach to primarily acquire songs over 10 years old, more than 90% of all the songs in the portfolio are 'vintage', written prior to 2000.

Exhibit 7: Portfolio breakdown by genre, Dec 20



Source: RHM

Exhibit 8: Portfolio breakdown by revenue type, Dec 20



Source: RHM

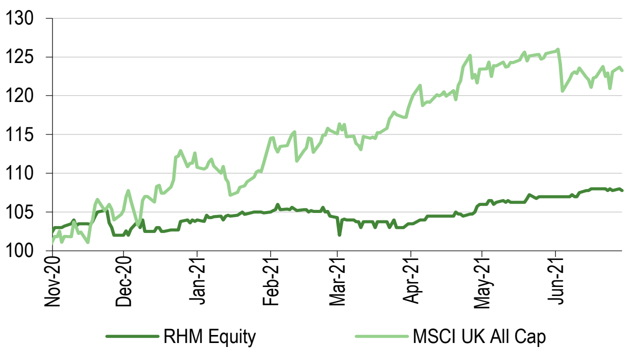
As shown in Exhibit 8, the portfolio is also diversified by revenue type, with nearly a quarter of the portfolio's revenues in masters' royalties.

Performance: Trading since 13 November 2020

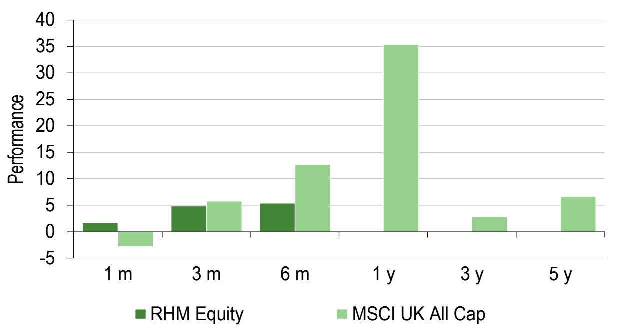
RHMRF's performance track record began on 13 November 2020, the first day of trading of the trust. RHMRF's share price is shown in absolute terms in the right-hand chart and in relative terms in the left-hand chart of Exhibit 9, compared to the MSCI UK All Cap Index.

Exhibit 9: Investment trust performance to 30 June 2021

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



Price, NAV and benchmark total return performance (%)



Source: Refinitiv. Note: Three-, five- and 10-year performance figures annualised.

Peer group comparison

Comparable funds

RHMRF is currently a constituent of the Association of Investment Companies' (AIC) Specialist sector: Royalties, alongside just one other London listed trust investing in music royalties: Hipgnosis Songs (SONG). The AIC's Specialist sector is very broad containing 14 other subsectors. As the other 13 subsectors are very different in business nature to music royalties, we have compared RHMRF with SONG, and also included the performance of the Barclays Global High Yield Index for performance comparison purposes. The lack of comparable peers only serves to underline the differentiation of RHMRF's revenue stream.

A comparison of RHMRF's and SONG's portfolios and attributes is covered in the appendix.

Exhibit 10: Selected peer group as at 30 June 2021*

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	SI** of RHM	Prem/disc (cum-fair)	Ongoing charge	Perf. fee	Net gearing	Dividend yield
Round Hill Music Royalty	254.0	N/A	N/A	N/A	(7.4)	**1.2**	1.95*****	Yes	109	4.5
Hipgnosis Songs	1,322.7	9.6	N/A	N/A	(1.2)	(2.5)	1.8	Yes	129	4.3
Simple average (2 funds)	788.4	9.6	**N/A**	**N/A**	(4.3)	**(0.7)**	1.9		126	4.4
RHM rank in peer group	**2**	**N/A**	**N/A**	**N/A**	**N/A**	**1**		**N/A**	**2**	**1**
Barclays Global High Yield Index		1.7	12.6	41.2	(1.8)					**5.5******

Source: Morningstar, Edison Investment Research. Note: *Performance based on cum-fair NAV. **SI = since launch. ***Simple average. ****12m yield to maturity average. *****Edison's estimate. TR = total return. Net gearing is total assets less cash and equivalents as a percentage of net assets, and in the case of funds investing directly in operating assets, does not include gearing at the underlying asset level.

RHMRF has the lower market capitalisation of the two funds. Both RHMRF's and SONG's track records are relatively short, with SONG launched on 11 July 2018, approaching its three-year anniversary. In performance terms, since launch RHMRF has lagged SONG on a share price total return basis, but we note the very short performance period of under eight months. It is typical for new funds to gain momentum over one year, as they establish themselves, invest and begin harvesting IPO proceeds, as RHMRF has done. This period largely reflects the set-up stage for RHMRF, as it has now fully invested its IPO proceeds and geared up.

In terms of the premium/discount to NAV, we believe it is too early to compare the two trusts, and the numbers in the premium/discount column in Exhibit 10 are indicative only. We note that SONG reported its latest economic (or operative) NAV per share ($1.6829) on 31 March 2021, and RHM is still to report one. RHMRF's economic NAV per share at launch was $0.98.

Given that the revenue streams from music royalties are defined by long-term contracts, they appear to be more predictable than those from renewable energy infrastructure businesses, where not all future prices are fixed over the long term. This possibly explains SONG's outperformance of both the renewable energy infrastructure businesses subsector and Barclays Global High Yield Index on a total return basis over one year and suggests a path for potential outperformance for the music royalties subsector, including RHMRF, going forward.

Ongoing charges are a little above average, and both RHMRF and SONG charge performance fees. Despite the royalties subsector's short-term performance record, it trades at a premium to NAV. RHM trades at a lower premium than its longer-established closest peer. RHMRF's gearing is lower than SONG's due to the trust's short existence. RHMRF's 4.5% prospective dividend yield is comparable to SONG's 4.3% historical 12-month yield but is lower than the index's yield.

Dividends and dividend policy

While it also aims for long-term growth of capital, RHMRF's primary objective is to reward its investors with a stable income. Following the completion of the second (since RHMRF's launch)

Investment, the directors anticipate paying the stated annualised dividend of 4.5% for the financial period to 31 December 2021. The first interim dividend of 0.0075c was declared in May 2021 and paid in June 2021. According to RHMRF, the first dividend was covered by income in the period to 31 March 2021

A number of factors highlighted in the NAV sensitivities and reporting section on page 11 will have an impact on RHMRF's income, including the company's ability to grow and scale up in the globally competitive environment. The prices paid to acquire catalogues, the discount rates and other factors used to value the assets will all play a role, and RHMRF's challenge is to balance these out to keep on track in delivering the targeted dividends and grow shareholders' capital. We expect RHMRF's board to clarify any revision to the dividend level in its first interim announcement for the six months ending 30 June 2021.

The dividend policy is to pay dividends on a quarterly basis: declare dividends for the quarterly periods ending March, June, September and December and pay in June, September, December and March respectively. The board targets an annualised dividend yield of 4.5% by reference to the issue price ($1.0). Dividends are aimed to be paid out of royalties income, but can be paid out of capital, if necessary, within the dividend policy.

Gearing: An RCF is being used

Maximum gearing allowed is up to 25% of the NAV. At end-June 2021 RHMRF's net gearing was 109% (defined as total assets less cash to net assets). RHM had $31m drawn on its $82m RCF.

On 4 May 2021 the board announced that RHMRF entered into a new RCF, provided by Truist Securities. The RCF allows the company to borrow up to 25% of economic NAV (defined in the RHMRF's prospectus as GAV less the fair value of liabilities and expenses of the company), calculated at the point of draw down. The RCF has been utilised to part finance the second investment, and the remainder may be used to acquire future pipeline opportunities.

Fees and charges

The investment manager is entitled to an annual management fee (payable in cash) and a performance fee (usually payable predominantly in ordinary shares, subject to an 18-month lock-up undertaking). The company pays the investment manager an annual fee payable quarterly in arrears, calculated as follows: 1.0% per annum of the average market capitalisation (over the relevant quarter) up to, but not including, $400m; 0.9% between $400m up to and including $700m; and 0.8% in excess of $700m.

Prior to RHMRF's first investment, completed on the 1 February 2021 (before 80% of the net proceeds of the Initial Issue was invested), RHM LP was receiving 50% of the management fee.

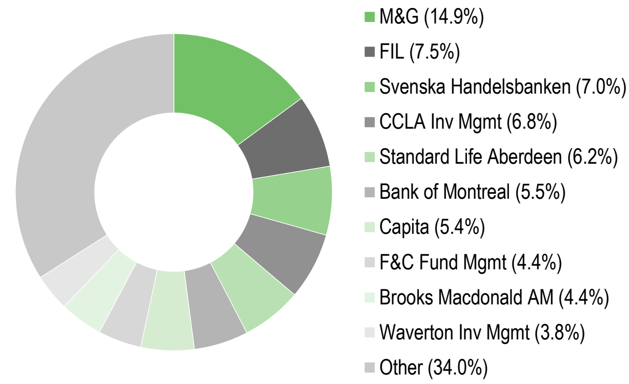
A performance fee is charged at 10% over excess total shareholder return (share price plus dividend), over either a hurdle (10% annual return, compounded, calculated from admission) or a high watermark (on the last share price when the performance fee was paid). The performance fee is paid in shares, subject to an 18-month lock up.

Edison estimates that ongoing charges are 1.95%.

Life of the company and ownership

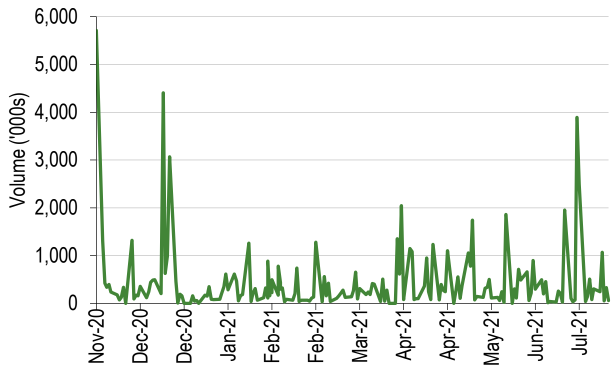
Structured as an investment trust, RHMRF has an indefinite life, is domiciled in Guernsey and is tax resident in the United Kingdom. The board proposed to hold a continuation vote after five years from IPO and every five years thereafter. The first vote is scheduled for 2025.

Exhibit 11: Major shareholders (ordinary shares)



Source: Refinitiv.

Exhibit 12: Average daily volume (ordinary shares)



Source: Refinitiv. Note: 12 months to end June 2021.

While RHMRF's major shareholders are currently institutional, close to 10% of the top 10 are held by retail investors (Exhibit 11). Retail investors presently hold c 25% of RHMRF's shares. Average daily trading volume on the London Stock Exchange since RHMRF's launch (Exhibit 12) was c 434,200 ordinary shares or c 0.13% of the share base.

The board

Exhibit 13: RHMRF's board of directors

Board member	Date of appointment	Remuneration in FY21	Shareholdings at end-H121
Trevor Bowen (chairman)	16 October 2020	£50,000 (pa)	75,000 shares
Caroline Chan	16 October 2020	£35,000 (pa)	50,000 shares
Francis Keeling	16 October 2020	£40,000 (pa)	20,000 shares

Source: RHMRF

Appendix

Comparison with Hipgnosis (SONG)

Exhibit 10 compares various features of RHMRF and SONG and illustrates the differentiation factors of RHMRF. Founded in 2010, RHM LP is a much longer established entity, compared with SONG's investment management group at just over three years' old. Round Hill has managed music royalty assets throughout all these years, while The Family (Music) acquired its song administration company in September 2020. Presently, both investment management groups have a comparable number of staff (55 for RHM LP and 88 for The Family (Music), respectively). We also note that SONG is the sole dedicated mandate for The Family (Music), while RHM LP currently has three funds, including RHMRF.

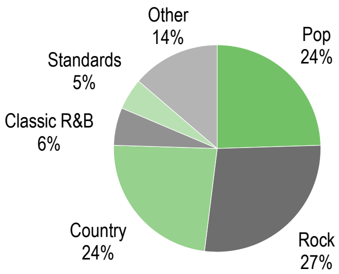
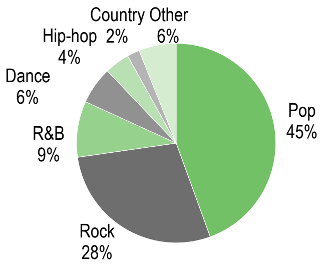
Exhibit 14: Features of RHM and SONG

Feature	Round Hill Music Royalty Fund (RHMRF)	Hipgnosis Songs Fund (SONG)
The manager	RHM LP, founded in 2010	The Family (Music) Limited (Merck Mercuriadis founded it in 2017)
Team	Over 55 music/finance professionals and administrators, based in New York, Los Angeles, London and Nashville	88 music/finance professionals and administrators, based in London, Los Angeles, New York and Nashville
The mandate	Specialist – music royalties	Specialist – music royalties
Launch date / Tenure	13 November 2020 / c 8 months	11 July 2018 / c 3 years
Investment strategy	Income & growth	Income & growth
Investment objective	To provide investors with an attractive level of regular and growing income and capital returns from investment primarily in high-quality music intellectual property	To provide shareholders with an attractive and growing level of income, together with the potential for capital growth, from investment in songs and associated musical intellectual property rights
Business model	In-house asset management	Used to be outsourced asset management, but song administration was moved in-house from September 2020
Target returns	The company is targeting a net total shareholder return of 9% to 11% per annum over the medium to long term	The NAV total return target is 10% per annum over the medium term net of fees and expenses
Dividend policy	The company targets an annualised dividend yield of 4.5%. Dividends are paid quarterly in March, June, September and December	At IPO, the company had a stated target dividend yield of 5% per annum, with the intention to grow this over time. In September 2020, the Board announced an increase in the target dividend to 5.25p/share. Dividends are paid quarterly in February, May, August and November
Performance fee	The performance fee is calculated as 10% of excess total returns relating to each accounting period	The performance fee is calculated as 10% of excess total returns relating to each accounting period
Ongoing charges	1.95% estimated	1.59% (from the annual report, year end 31 March 2021)
Currency	Do not currently hedge currency risk. The share capital and dividends are denominated in US dollars.	Does not currently hedge its currency risk. Share capital is denominated in sterling and it pays dividends in sterling. Changed its functional and presentation currency from sterling to dollars with effect from 1 October 2020
Gearing	Max up to 25% of economic NAV** (was c 9% at end-June 2021 via draw-down RCF).	Max up to 30% of operative NAV** (was c 29% at FY end-March 2021 via draw-down RCF). NB in its annual report for FY21 the company disclosed breaching its gearing policy between 26 March and 5 April 2021, with gross gearing temporarily going up to 32.8%. RCF is $600m

Source: Company documents, Edison Investment Research. Notes: TA = total assets, *KID = key information document. **Economic NAV = net asset value (for RHM) and operative NAV (for SONG) is the external valuation of assets, not IFRS numbers.

RHMRF is slightly more conservative with its dividend target of 4.5c per share (amounting to a c 4.5% dividend yield), compared with a 5% dividend yield target for SONG.

Exhibit 15: Portfolio comparison

Portfolio	Round Hill Music Royalty Fund (RHMRF)	Hipgnosis Songs Fund (SONG)
Date	**31 December 2020**	**31 March 2021**
No of catalogues and songs	39 catalogues with over 118,000 songs. To end-June 2021 this consisted of two distinct parts: 1) First investment: 38 catalogues, containing over 18k songs; 2) Second investment: over 100k songs in one catalogue	138 catalogues with over 64,000 songs
Fair value	c $342m (based on acquisition value)	$1.8bn
Weighted average acquisition multiple, NPS (x)	16.2x	15.3x
By genre (est.)		
By age (estimated)	0–3 years: 2%; 3–10 years: 3%; 10+ years: 95%	0–3 years: 3%; 3–10 years: 37%; 10+ years: 60%
By revenue source	Performance: 37%; Master royalties: 23%; Synchronisation: 23%; Mechanical: 14%; Other: 3%	Streaming: 32%; Performance: 29%; Synchronisation: 15%; Mechanical/Master royalties: 17%; Other: 4%; Digital downloads: 3%
Average portfolio song's % ownership	Majority of catalogues are 100% owned, only 12 catalogues have ownership of between 50–99%	Most catalogues are 100% owned; less than 10 catalogues have ownership of between 50–99%
Current pipeline	Over $420m	c £150m (c $210m)
Investment limits	Min 15 catalogues	Min 300 songs
	Min 5,000 musical compositions	Max 5 % GAV in advance payment to songwriters for future acquisition of royalties
	Single song copyright value at max 20% GAV	Single song copyright value at max 10% GAV
	Single songwriter copyright value at max 25% GAV	
	Copyrights <5 years old at max 20% GAV	
Investment policy	Target to acquire a 100% of a songwriter's copyright interest in a song and/or catalogue, including three major elements: writer's, publisher's and performer's shares	Target to acquire a 100% of a songwriter's copyright interest in a song and/or catalogue, including three major elements: writer's, publisher's and performer's shares
	May (and often) acquire a lesser or minority copyright interest	May (and often) acquire a lesser or minority copyright interest
	Create value by efficient royalties collection and active management of the owned songs (both elements are in-house, RHM LP has over 10 years' experience)	Create value by efficient royalties collection and active management of the owned songs (both elements were outsourced, but now moved in-house). Hipgnosis Songs Group (HSG), the song administrator, formerly Big Deal Music, was acquired by SONG in September 2020
	Predominantly invest in small to medium sized catalogues (typically 100–1,000 copyrights) that are diversified by artist, genre, decade and royalty type and were purchased directly from songwriters. Focus on classic, older copyrights with enduring appeal and which experience consistent usage (eg pop and rock)	Focus on building a diversified portfolio, acquiring catalogues that are built around proven hit songs of cultural importance by some of the most talented and important songwriters globally

Source: Company documents, Edison Investment Research

RHMRF has thus far made two investments (the first and second, discussed above) in catalogues. We note that although the average number of the songs in each catalogue (c 3,000) is almost sixfold higher than in SONG (c 450), this is statistically skewed towards the second investment. The bulk of RHMRF's current portfolio (82% by total capital invested of $342m to end June 2021) consists of the First investment, which is 38 catalogues, containing over 18k songs, or 474 songs per catalogue), which is similar to SONG's average catalogue size.

RHMRF's portfolio is more mature by age: 95% of its catalogues' songs are over 10 years old, compared to 60% at SONG. Bearing in mind the recent flotation of RHMRF in November 2020, we note its healthy pipeline of c $420m. This compares with the c $210m pipeline for SONG, which is more mature at three years old.

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