APQ Global

Update on progress

Meeting income targets and looking to grow

Financial services

APQ Global is well on track to deliver its targeted 6% yield on its August 2016 IPO price of 100p. The proceeds from the IPO and follow-on CULS issue have initially already been invested in a highly diversified liquid markets portfolio of mainly global emerging market bonds and equities, including a number of strategic positions. APQ continues to work on the sourcing of direct investments. The management team is experienced and incentivised, and supported by an advisory group of international EM experts. It aims to deliver a sustainable, progressive dividend with the potential for capital growth from investments in emerging markets.

Year end	EPS (p)	NAV/share** (p)	DPS*** (p)	P/E (x)	P/NAV (x)	Yield (%)
12/16*	0.71	99.2	0.5	N/A	1.02	0.5
12/17e	N/A	96.3	6.0	N/A	1.05	5.9

Note: *Period commencing at inception on 11 August 2016 until 31 December 2016. **12/17e NAV is last reported as at 31 October 2017 and is ex the 1.5p dividend paid on 27 November 2017. ***Management target dividend for current year.

Income returns on track; further CULS issue

APQ has paid three quarterly dividends year to date, or an aggregate 4.5p, and says it is comfortably on track to meet its 6.0p full year DPS target, well covered by economic earnings. The £20.1m proceeds from the August 3.5% CULS issue have already been invested, representing around half of the c 50% increase in Q3 asset exposure as a percentage of book value. Despite the increase, management indicates that its investment stance remains cautious and income focused, and its updated sensitivity analysis shows that expected book value sensitivity to market movements remains low. An EGM will be held on 21 December in relation to a further issue of CULS, which management believes will provide additional long-term financing for further investment at an attractive fixed cost.

Targeting long-term EM income growth

APQ's strategic objective is to build a growing business in emerging markets (EM) globally as well as earning revenue from direct investments in income-generating operating activities. Against the backdrop of secular growth opportunities in emerging markets, the company's goal is to steadily grow earnings and deliver a sustainable and growing dividend to shareholders with added potential for capital growth. Unlike a typical emerging markets fund, APQ is targeting absolute returns and growth rather than performance relative to any specific asset class or index. Plans for direct investment with management control are a clear differentiator. The management team is highly experienced and its interests are strongly aligned with those of shareholders. CEO Bart Turtelboom invested c £22m at the IPO and is a c 28% shareholder in APQ.

Valuation: Attractive targeted yield

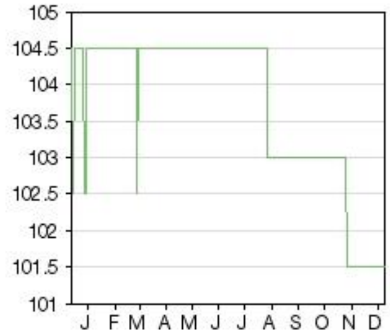
The targeted FY17 DPS represents a yield on the current share price of 5.9%. Of less relevance given APQ's income focus, the shares trade at a 5% premium to last reported book value. Management is targeting long-term sustainable EM income growth while seeking to mitigate the risks of market volatility.

11 December 2017

Price	**101.5p**
Market cap	**£79m**

Company net cash (£m) at 30 June 2017 (excludes cash held for working capital purposes within unconsolidated APQ Cayman subsidiary)	0.2
Shares in issue	78.055m
Free float	7.8%
Code	APQ
Primary exchange	TISE
Secondary exchange	AIM

Share price performance



%	1m	3m	12m
Abs	0.0	(1.5)	(2.9)
Rel (local)	1.8	(2.0)	(10.1)
52-week high/low		104.8p	101.5p

Business description

APQ Global is an emerging markets investment company with a focus on Asia, Latin America, emerging Europe, the Middle East, and Africa. It aims to deliver a sustainable and growing dividend as well as capital growth for shareholders by focusing on investment opportunities with the potential to generate significant income and long-term growth.

Next events

EGM	21 December 2017

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Edison profile page

APQ Global is a research client of Edison Investment Research Limited

Company description

APQ Global ("APQ") is an emerging markets company with a focus on Asia, Latin America, emerging Europe, the Middle East, and Africa. It aims to deliver a stable and growing dividend and capital growth for shareholders by focusing on generating significant income from business opportunities with good value and long-term growth potential. The focus on income reflects the managers' view that investors in emerging markets tend to overpay for the 'dream' of long-term growth and underpay for the cash flows readily coming from the asset class. APQ initially targeted a dividend yield of 6.0% on the IPO price of 100p for the year ending 31 December 2017 (FY17), its first full year of trading since IPO, and management indicated in its Q3 update that it is comfortably on track to meet this, with dividends well covered by economic earnings. A dividend of 0.5p per share was paid in February 2017 in respect of the short FY16 financial year and three quarterly dividends, each of 1.5p per share, in respect of FY17 have been paid year-to-date.

APQ is still a relatively new company, having listed on the International Stock Exchange (TISE) in Guernsey little more than a year ago in August 2016. It raised c £78m in new equity capital at IPO and it was admitted to trading on the London Stock Exchange AIM Market two weeks later. In August 2017 APQ issued £20.1m in new 3.5% convertible unsecured loan stock (CULS) maturing in 2024, which increased investable funds to c £100m. The CULS are listed on the International Securities Market of the LSE. As discussed below, APQ has recently announced its intention to expand the CULS issue.

The APQ management team brings considerable emerging markets experience and have worked together for a number of years. They all joined the company through the acquisition of APQ Partners LLP, of which they were all co-founders in 2013, and which was acquired by APQ Global in January 2017. Before jointly founding APQ Partners LLP, they worked together at GLG. The team is led by CEO Bart Turtelboom, who invested c £22m at the IPO and is a c 28% shareholder in APQ, strongly aligning his interests with those of shareholders. The management team is assisted by an advisory group, the International Advisory Council (IAC), a geographically spread group of emerging markets specialists, whose main role is to provide valuable insights and market intelligence from around the world with a secondary objective of helping to raise the market profile of the company.

For an in-depth description of the company's strategy, the management team and its track record, and the IAC, please see our initiation note.

Portfolio update

The c £20.1m in proceeds from the CULS issue, representing a c 25% increase in APQ's funds for investment, had been deployed by the end of September 2017, when the company remained fully invested except for cash retained for collateral and working capital purposes.

Exhibit 1: Portfolio breakdown as a percentage of book value

	30 September	30 June
Credit & government bonds	60.7%	55.0%
EM local markets	16.2%	13.5%
Equities	60.4%	22.6%
Cash	13.4%	10.0%
Total	**150.7%**	**101.1%**

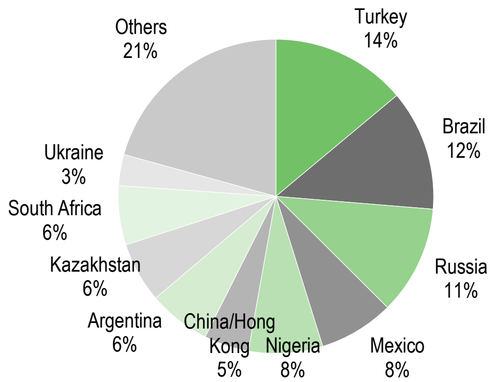
Source: APQ

Exhibit 1 shows the portfolio asset class exposures as a percentage of book value. This has increased since the half-year stage by c 50%, of which roughly half represents the deployment of the CULS proceeds, which do not add to book value (equity) but do increase funds for investment, and the balance of exposure representing a general, planned increase in position taking. Management believes that the political headwinds from developed countries have eased and expects macroeconomic developments to remain favourable for EM with emerging markets remaining the main drivers of global GDP growth. At the same time, inflation dynamics are diverging between EM and developed markets; with inflation on an upwards trend in developed markets and tapering off in EM. In this context, APQ anticipates that EM currencies may weaken but that this is likely to open up significant opportunities. As we explain below, although APQ has deliberately increased asset exposure, and quite significantly compared with end-Q2, it has sought to retain a cautious stance with regard to market risk (see Exhibit 6). Exposure has increased to all asset classes with credit (hard currency denominated corporate credit) remaining the single largest exposure. Equity exposure showed a notable increase during the period.

During Q3 the direct currency exposure (ie currency exposures beyond those arising from the equity portfolio) was increased significantly. The existing long position in the Turkish lira was increased from 6.5% of book value at end-Q2 to 17.7%, while positions were also established in the Brazilian real (11.8%), the Polish zloty (11.8%), and the Indian rupee (9.9%).

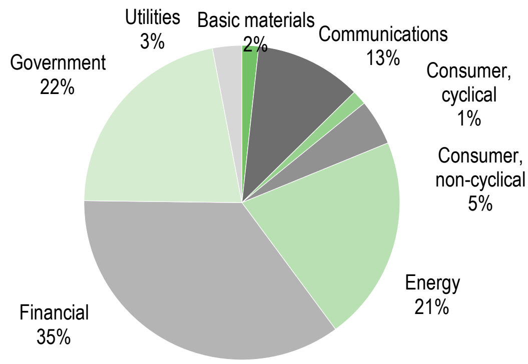
Looking more closely at the individual asset classes, the substantial credit exposure remains well diversified by borrower, geography, and sector, with the intention of smoothing out volatility and providing stable income. The largest single exposure at 30 September was to Mexican state-owned petroleum company Pemex, at 2.0% of overall book value (30 June: VTB Bank, a leading Russian universal bank, at 1.1% of book value). The country and sector credit exposures are shown in Exhibits 2 and 3 below.

Exhibit 2: Credit exposure by country as at 30 September 2017



Source: APQ

Exhibit 3: Credit exposure by sector as at 30 September 2017



Source: APQ

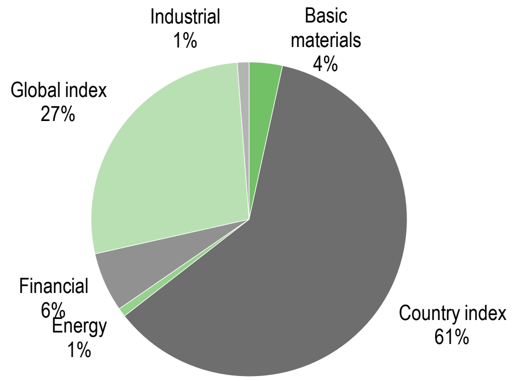
Geographically, the largest exposure at 30 September was to Turkey at c 14% of book value, moving above Russia and Brazil, which represented the largest exposures at 30 June. Sector-wise, credit exposure is concentrated in government entities, banks and corporations in the energy and materials sectors.

In Exhibit 4 we update the list of the top 10 equity holdings. This list includes holdings in City of London Group and Anglo Pacific that management considers as “strategic” holdings in the sense that it has identified a particularly compelling multi-year investment case. Its intention is to act as a longer-term constructive shareholder or lender.

Exhibit 4: Top 10 equity exposures as at 30 September 2017	
Exposure as % of book value	
MSCI EM Index	16.1%
Russian Depository Index USD	5.3%
City of London Investment Group plc	3.6%
Anglo Pacific Group plc	1.1%
Rio Tinto plc	0.9%
Cemex SAB de CV	0.7%
Gazprom PJSC	0.5%
BHP Billiton	0.5%
Anglo American plc	0.3%
Vale SA	-0.7%
Total top 10	**28.3%**
Other	32.1%
Total equity exposure	**60.4%**

Source: APQ

Exhibit 5: Equity exposures by sector as at 30 September 2017 (% of book value)



Source: APQ

Overall book value exposure to the top 10 holdings has doubled since June, although this is a smaller increase than equity exposure as a whole, which has increased from 22.6% to 60.4% of book value. Within the top 10 holdings, exposure to the MSCI EM Index has increased by c 11%, while nine of the top 10 holdings were also within the top 10 at 30 June.

Leaving aside these strategic holdings, the largest EM equity positions remain concentrated in Russia, reflecting management's view that the global economic growth outlook will continue to be supportive of commodity markets and that Russia offers compelling value. From a sector perspective and taking into account the index exposures in Russia, India, and global EM, the main equity exposures are to industrials and financials.

Global emerging equity and debt markets have been strong over the past year, but although management is very optimistic about the medium-term prospects for emerging markets, it is wary of the potential for global political uncertainties and the tightening in US interest rates to create near-term volatility. With ample liquidity compressing risk premia across global markets, including EM, APQ management sees a distinct lack of value and has continued to maintain liquid exposures with a focus on income. This approach insulated shareholders from an aggressive EM sell-off in the aftermath of the US presidential election in Q416 and APQ management anticipates further volatility in the months to come, from which it believes it is well positioned to identify attractive investment opportunities that will generate long-term sustainable income growth.

Although market risk exposure has been deliberately increased as a result of the c 50% increase in asset exposure, management believes that book value sensitivity to overall market movements remains low. To support this, it updated its unaudited stress test scenario results at Q3 as shown in Exhibit 6.

Exhibit 6: Management stress test results – predicted change in book value

Scenario	30 September	30 June
Equity stress test (S&P -10%)	-0.38%	0.28%
Credit stress test (credit spreads +10%)	-0.93%	-0.62%
Interest rate stress test (yields +1%)	-1.02%	2.58%

Source: APQ

The internally conducted stress test takes into account the portfolio positioning as at a given period in time as well as historical correlations between asset classes. The analysis indicates that although equity exposure significantly increased during Q3, if the S&P 500 equity index were to decline by 10%, the impact on book value would still be relatively small at a negative 0.38% compared with a positive 0.28% at end-Q2. Similarly, the predicted negative impacts of an increase of 10% in the level of credit spreads (over Libor) and an overall increase in yields of 1% have increased since end-Q2, but are not significant.

Update on statutory results

APQ publishes monthly unaudited NAV updates, quarterly strategic and portfolio updates, and has published its statutory results for the short year to 31 December 2016 and interim results to 30 June 2017 in respect of the current financial year. However, at this stage of the company's development there remains insufficient data upon which to build financial forecasts.

Exhibit 7: Summary of statutory financial statements

Year end December (£000s)	2016	H117
INCOME STATEMENT		
Net gains on investment	965.5	(315.2)
Dividend income from unconsolidated subsidiary	0.0	1,770.8
Expenses	(412.5)	(931.4)
Profit before tax	552.9	524.2
Tax	0.0	0.0
Net attributable profit	**552.9**	**524.2**
Closing shares in issue	78.1	78.1
Average shares in issue	78.1	78.1
EPS (p)	**0.71**	**0.67**
DPS – declared basis (p)	**0.5**	**1.5**
BALANCE SHEET		
Investments at fair value through P&L	76,595.7	76,280.6
Cash & equivalents	913.5	186.3
Total assets	**77,509.2**	**76,466.9**
Payables	(116.6)	(111.2)
Net assets	77,392.6	76,355.7
NAV per share (p)	**99.2**	**97.8**
CASH FLOW		
PBT	552.9	524.2
Adjust for:		
Net gain on investments	(965.5)	315.2
Increase in creditors	116.6	(5.5)
Cash flow from operating activity	(295.9)	833.9
Acquisition of investment in APQ Alexandria	(58,500.0)	0.0
Cash flow from investing activity	(58,500.0)	0.0
Proceeds from initial share issue	60,924.8	0.0
Cost of equity issuance	(1,215.4)	0.0
Dividends paid	0.0	(1,561.1)
Net cash flow from financing activity	59,709.4	(1561.1)
Net change in cash	**913.5**	**(727.2)**
Opening cash	0.0	913.5
Closing cash	**913.5**	**186.3**

Source: APQ Global

The company operates through two main subsidiaries, wholly owned APQ Cayman Ltd (APQ Cayman), and 98% owned APQ Partners LLP (APQ Partners). APQ Cayman is the vehicle through which the group's investments to date have been made and where the group's counterparty trading arrangements reside. Although wholly owned, it is treated as an "investment entity" under IFRS 10 and is accounted for as an investment held at fair value with gains and losses taken as a single line entry through the group P&L. Although this structure provides operational benefits to the group, it does limit the usefulness of the group statutory financial statements.

APQ Partners is the group's asset management subsidiary. It was formed by Bart Turtelboom and others to manage the APQ Alexandria Fund, a Cayman Islands registered fund investing in a wide range of assets across global emerging markets from its inception in 2013. At the listing of APQ Global, c £17m of the £78m raised was used to acquire APQ Alexandria, effectively at net asset value, and APQ Alexandria was renamed APQ Cayman Limited. At the same time, APQ Partners became the asset manager for APQ Global and once all of the regulatory permissions had been granted post-IPO, it was acquired for a nominal sum and the management of APQ Global was internalised.

The returns generated by the subsidiaries, net of remittances to APQ Global, primarily to support dividend payments, are reported as net gains/losses on investment. In H117, remittances were £1.8m and the resulting net loss on investments was £315k. Management has indicated that the high level of expenses in H117, equivalent to an annualised rate of 2.4% of average assets, includes a significant non-recurring element of c £400k related to IPO expenses that had been incurred by APQ Partners and recognised on acquisition of the latter. Adjusting for this, the annualised recurring expense ratio was c 1.4%, a similar expense ratio to the short FY16 trading period, although this included some impact from IPO-related and set-up costs.

The c £20.1m in CULS were issued after the period end (in August) and the proceeds have since been invested. For as long as the returns generated on this additional investment exceed the 3.5% cost of the debt, the impact should be to reduce the cost-asset and cost-income ratio. APQ will hold an EGM on 21 December in connection with a potential further issue of the existing series of 3.5% CULS. The board is seeking shareholder approval to disapply the pre-emption rights set out in the company's articles of incorporation in relation to the grant of rights to convert the CULS into ordinary shares in the capital of the company. APQ believes that further CULS issuance is the best way to finance the continued development of the company’s portfolio. Since being issued at a price of £5,000 per £5,000 nominal, the market price of the first CULS tranche has increased to £5,375 (as at 30 November 2017) such that further CULS issuance would have a lesser dilutive impact on non-participating ordinary shareholders than an equity issue. It is anticipated that the new CULS issue will similarly pay 3.5% on the nominal value and will have a similar conversion entitlement to ordinary shares on a quarterly basis throughout their life (expected to be until September 2024) at a price of 105.358p. The conversion premium is a 10% premium to the book value per ordinary share as at 31 July 2017.

The dividends paid during H117 include the 0.5p per share paid in respect of FY16 and the first of the three quarterly dividends of 1.5p each that have been declared year to date in respect of the first nine months of FY17.

Given the challenges in interpreting the statutory reporting, in the next section we consider the NAV total return performance up to and including the most recently published unaudited NAV as at 31 October 2017.

Performance and valuation

The targeted dividend yield in respect of the current year of 6.0% on the 100p issue price represents a prospective 5.9% dividend yield based on the current 101.5p ordinary share price. Management indicated in its Q3 update that it was comfortably on track to meet the full year DPS target, which it said was well covered by economic earnings. Economic income is a forward-looking measure based on current yields on bond and equity investments as well as more complex measures such as the notional yield embedded within FX forward contracts and hedges.

The most recent NAV per share is 96.3p as at the end of October 2017. Between listing at 100p in August 2016 and the end of October 2017, an aggregate 3.5p in dividends per share had been paid (an additional 1.5p per share was paid in late November), which means that dividend distributions have very slightly exceeded IFRS total comprehensive income over the period. When management indicates that targeted distributions are well covered by economic earnings, the key differences with the statutory accounting measure are:

- The forward-looking nature of the economic income measure.

- Translation differences between the functional currency (US dollars) in which the company's assets are managed and the reporting currency (sterling) in which it reports.
- One-off costs related to the IPO and CULS issuance.

In Exhibit 8 we show the monthly NAV total return performance with dividends reinvested from inception up to and including end-October 2017.

Exhibit 8: Monthly change in APQ NAV per share (dividends reinvested)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Ytd
2016									1.46%	-0.43%	-1.22%	-0.59%	-0.80%
2017	-1.25%	0.24%	-0.48%	-2.12%	3.15%	1.17%	-0.54%	0.72%	0.45%	-0.64%			1.42%

Source: APQ, Edison Investment Research

We estimate that 2017 year to date sterling denominated NAV total return performance is 1.4%. To provide context, in Exhibit 9 we show the H117 performance calculated in sterling for a range of global equity indices and iShares EM bond ETFs. However, we note that APQ's strategy positions it quite differently to both the index and the EM fund sector. APQ is focused on identifying and targeting investments with the potential to provide an attractive and growing income stream with no consideration given to emerging markets indices. It has unconstrained investment flexibility across asset classes, long and short, with only prudential limits on gearing, and over time it is management's intention to make direct investments, potentially consolidating these into the group financial statements.

Exhibit 9: Comparator bond and equity performance year to date (as at 31 October 2017)

iShares Emerging Markets Corporate Bond ETF	-3.61%
iShares US$ Emerging Markets Bond ETF	-1.93%
iShares Local Currency Emerging Markets Bond ETF	1.59%
MSCI EM Index (total return)	23.42%
MSCI World Index (total return)	10.50%
FTSE All Share Index (total return)	9.76%

Source: Bloomberg. Note: All sterling equivalents.

In its Q3 update, APQ provided the breakdown of its FY17 year to date performance by asset, shown in Exhibit 10. There has been a broad spread of positive contributions across asset classes with the exception of FX.

Exhibit 10: Return contribution by asset class (1 January to 30 September 2017)*

	Year to date	Q3
Credit	2.5%	0.8%
Equity	2.1%	1.4%
FX	-3.1%	-2.0%
Rates	2.1%	0.2%
Total	**1.3%**	**1.6%**

Source: APQ. Note *Dividends paid have been added back but no reinvestment assumed.

At this stage in the company's development, we believe that investors are likely to draw comparison with emerging markets in general and the emerging markets fund sector, focusing on book value performance and yield. Using Morningstar data for a grouping of more than 20 EM closed-end funds in the global categories of EM equity and EM fixed income, the average price discount to NAV is c 9.0% with an average yield of 1.4%.

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