VT UK Infrastructure Income Fund

Background note

Investment Philosophy

The VT UK Infrastructure Income Fund 'UKIIF' has capital preservation coupled with income as its primary target. The underlying investments of the fund are securities which invest in or own contracts where the free cash flow yield is derived from either long-term contracts with the public sector for the provision of core services or from commercial entities providing core services within highly regulated and quasi monopolistic frameworks.

UKIIF Strategy Aims

- 5% yield after charges
- Capital preservation coupled with modest capital growth
- Low volatility and correlation to other asset classes
- Inflation protection with cash flows
- Sterling denominated listed UK Infrastructure sector holdings
- Low portfolio turnover

Key Risk Parameters for the Strategy

- Minimum of 75% of the portfolio is supported by UK Government backed cash or regulated cash flows
- Minimum of 80% of portfolio invested in completed/operational assets
- 100% allocation to sterling denominated securities
- Minimum 80% 'availability' based (rather than 'demand' based) projects. 'Demand' based projects, such as toll roads generate revenues per user. 'Availability' based assets, such as hospitals, generate revenue based upon a statutory and often UK Government backed cash flow
- Minimum of 22 holdings. Currently, there are 29 holdings, creating total underlying exposure to over 1000 separate underlying projects
- Majority of cash flows linked to inflation

The Investment Process

Investments are selected for inclusion in the Fund based upon several key factors:

- Capital preservation
- Yield sustainability
- Size/liquidity
- Inflation hedging characteristics
- Sustainable valuation
- Low relative volatility

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Available on the following platforms

7IM	James Hay
Aegon	Novia
AJ Bell	Nucleus
Alex	Old Mutual (Skandia)
Allfunds	OM Wealth
Alliance Trust	Pershing
Ascentric	Prudential*
Aviva	Raymond James
Axa Elevate	SEB International Life (Dublin)*
Canada Life (Dublin)*	SEI
Cofunds	Standard Life
FNZ	Stocktrade
Fidelity FundsNetwork	Transact
James Brearley	True Potential

*Offshore Bond wrappers

Suitable for:

Direct investors	Offshore bonds
SIPPs	Companies
ISAs	QROPS
Charities	

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UKIIF Financial Highlights – 25th January 2016 to 31st March 2017

- Assets under management of £162m as at 31/3/17
- UKIIF portfolio turnover to 31st March of 3.86%

Dividends paid per £1000 invested

Dividends	May 16	Aug 16	Nov 16	Jan 17	Apr 17	Total Income	Total Return
UKIIF C GBP Income	£6.61	£10.99	£15.49	£12.85	£9.55	£55.49	£1,141.74
UKIIF I GBP Income	£8.03	£11.47	£16.00	£13.33	£10.05	£58.88	£1,142.30

Returns indices

	Mar 17	3 Months	6 Months	12 Months	Since Inception
UKIIF*	0.75%	2.18%	3.54%	11.46%	13.95%
MSCI UK	1.17%	3.79%	8.14%	23.50%	31.26%
MSCI World	0.58%	5.12%	12.56%	31.92%	42.56%
MSCI Global Infrastructure	0.81%	2.78%	5.10%	19.49%	32.12%
Gilts	-0.17%	1.30%	-3.10%	4.08%	6.61%

Correlation, Performance & Volatility Comparison

	Correlation	Return	Volatility	Yield
UKIIF*	—	14.0%	5.2%	4.4%
MSCI UK	0.43	31.3%	14.8%	3.9%
MSCI World	-0.01	42.6%	13.0%	2.4%
MSCI Global Infrastructure	-0.08	32.1%	13.5%	3.9%
UK 10 Year Gilts	-0.23	6.6%	7.4%	1.1%

* VT UK Infrastructure Income Fund GBP C Acc. Past performance is not necessarily a guide to future performance

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Drawdowns

	Drawdown	Start	End	New High	Fund During Drawdown
UKIIF*	-3.04%	29 Apr 16	27 Jun 16	04 Jul 16	—
MSCI UK	-8.81%	29 Jan 16	11 Feb 16	29 Feb 16	-1.84%
MSCI World	-7.54%	29 Jan 16	11 Feb 16	23 Feb 16	-1.84%
MSCI Global Infrastructure	-8.66%	17 Oct 16	14 Nov 16	30 Dec 16	-1.14%

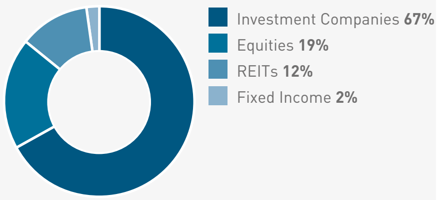
* VT UK Infrastructure Income Fund GBP C Acc. Past performance is not necessarily a guide to future performance

Top 10 holdings

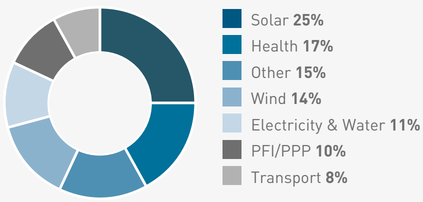
Company	%
Bluefield Solar Income Fund Ltd	8.6
GCP Infrastructure Investments Ltd	8.3
Renewables Infrastructure Group Ltd	8.0
MedicX Fund Ltd	6.1
Foresight Solar Fund Ltd	5.5
John Laing Environmental Assets Group Ltd	4.6
NextEnergy Solar Fund Ltd	4.5
Greencoat UK Wind PLC	4.5
Target Healthcare REIT Ltd	4.4
SQN Asset Finance Income Fund Ltd	4.0

Portfolio

Sectors



Underlying Project Exposure



Note on Current Valuations for the UK Infrastructure Sector

In the closed ended investment companies we see excellent value across the best firms as they continue to acquire long dated cashflows at high single digit returns with upward only inflation linkages. In the renewables sector the best operators are acting as consolidators, as industry and EIS owned facilities, for example, continue to be sold to lock in the developer returns; as yet despite persistently low bond yields, yields at purchase here are not under pressure. Discount rates being used to generate NAVs remain conservative as they are set by Boards or external consultants and vary in the 7.5% to 8.75% range. Modest leverage is being applied to these portfolios taking advantage of the availability of extremely low, long term fixed rate debt offered by UK pension funds and insurers (in the 3.00% area) which further enhances returns for investors. The backdrop is similar in the pure Infrastructure names; with increased government focus on infrastructure stimulating asset production and again reducing any downward market pressure on rates at which assets are acquired. Across all the closed end investment companies two additional value aspects stand out: the first as noted in the inflation linkage which is already having an effect – for example Bluefield Solar's NAV increased 5.6% over the six months to 31/12/16 with inflation adding c 50% of this; the second is that as the companies place shares to finance new acquisitions, VTUKIIF as an aggregator is able to acquire a significant amount of its requirements in this manner which significantly reduces premiums to the (conservative) NAVs – and in aggregate the fund has saved 68.5 bps in this way since launch (vs pre announcement share prices).

In REITs similarly, we continue to find compelling value in primary healthcare such as GP surgeries, well run care home portfolios and some student accommodation funds. Yields for these long term lease assets remain well above those achievable for similar risks in the bond markets, given the best managers work hard to put together portfolios of assets (which individually lack scale) and again modest long term leverage provides an excellent boost for investors. We recently invested in the Impact Healthcare IPO, an existing portfolio yielding 6% from day one with capital growth potential which is already reflected in the price performance.

In bonds the assets that we bought have done particularly well, with some gains from general price appreciation and a good amount of alpha stemming from the research driven approach identifying value opportunities, such as in RWE (Innogy Finance) before its reorganisation. However, at present as noted, QE has pushed bonds to a level where opportunities are few and value is scarce and our allocation is presently at its lowest since launch. Our only purchase in recent months being an issue backed by the PPI financing of the major hospitals in Peterborough, which continues to perform very well.

Equities (mainly utilities) as a whole comprise less than 20% of our portfolio. Global developed markets equities look fully valued but we believe predictably regulated utilities with strong regulated asset bases and broad customer profiles offering yields between 4% and 6% with steady capital performance remain compelling value propositions at this level of portfolio concentration.

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Risks associated with investing in UK Infrastructure

Inflation – Infrastructure assets are expensive and are often paid for over an extended period of time, backed by public sector cashflows. Private sector infrastructure projects such as renewables are generally subsidised by Government backed subsidies. The long dated nature of these concessions exposes the recipient to the risk of inflation and to mitigate the impact, the cashflows are often linked to inflation. Government subsidies are reset annually in April, upwards only, to take account of RPI, meaning the cashflow arising increases to the equity owners. Additionally, the Net Asset Values of the equity owners inflate during periods of elevated inflation. For example, HICL assume the long term RPI rate to be 2.75% per annum. A divergence of 1% above or below will increase or decrease the Net Asset Value of the Company by 6% per annum.

Lenders to infrastructure projects benefit from 'principal indexation' using the annualised RPI or CPI figure as their benchmark. The principal of the loan can increase annually, above a pre agreed 'strike price'. The interest rate for the loan remains the same but the principal rises, ensuring the lender benefits in times of elevated inflation. These contracts are upwards only and for the life of the loan.

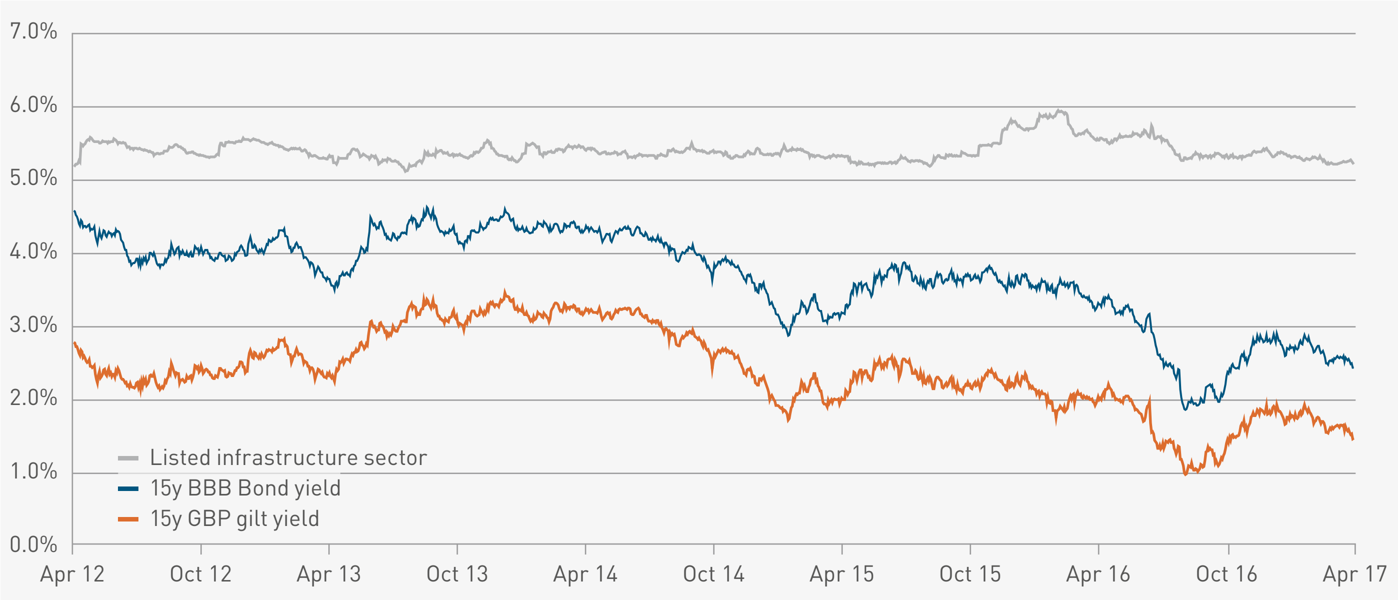
Counterparty – As with other asset classes, there is the possibility of a counterparty defaulting within an infrastructure project. However, as many projects are supported by the UK public sector, the risks are considered to be very low. Although such a default could adversely affect the income received by the fund and impact the value of the fund's assets, it is worth noting that since this form of financing was introduced in 1994, impairments and defaults have been very rare and the corresponding impact negligible.

Regulatory – In the UK, all projects built under the Private Finance Initiative (PFI), now called PF2, and all subsidies supporting the installation and operation of renewable energy projects are protected under the Infrastructure Act 2015. Since its introduction in the early 1990s PFI and PF2 have enjoyed the support of central Government. The Government could initiate new law amending previous Acts of Parliament, however, the Government has a stated target for expenditure of £500bn and it is anticipated that 2/3 will come from the private sector. It is considered unlikely that the Government would amend this legislation and for fear of deterring the private sector.

The impact of rising Government Bond Yields on the UK Infrastructure Sector

The graph below shows the historic movements of 15 year BBB GBP corporate bond yields, 15 year gilt yields and infrastructure sector yields. Whilst there is a correlation between the long dated credit markets and the infrastructure sector, there is a weaker relationship between the infrastructure sector and corporate bonds and a negative correlation to Gilts. It can be seen from the graph below that this is evident in both strengthening and weakening credit markets.

It is worth noting the current spread between gilts and infrastructure yields is high by historical standards, suggesting a 'buy signal' for the sector.



Source: Bloomberg

VT UK Infrastructure Income Fund

Background Note

UK Infrastructure investment company premiums to Net Asset Values (NAV)

- Companies in the infrastructure sector are structured similarly to Investment Trusts, which enables these companies to invest in or buy and hold illiquid assets with long dated cashflows attached. The lack of liquidity, eg lack of trading in the underlying holdings presents a problem for the valuation agents, who have little real data on which to calculate the Net Asset Value of each of these Companies. They are inclined to err on the side of caution and undervalue (rather than overvalue) these portfolios. The market must then decide the 'correct' price at which it is willing to buy and sell the equity of security.
- As evidenced by the examples below, on the rare occasions when infrastructure funds dispose of assets, they have done so at substantial premiums, not only to the NAV, but also to the implied valuations demonstrated by the share price. Such historic disposals support the case of infrastructure NAVs significantly underestimating the true, realised value within portfolios.

  "HICL Infrastructure Company Limited has sold its 56% equity and subordinated debt interest in the Colchester Garrison MoD Project… £21.7m above the directors' valuation of £86.6m as at 30 September 2014."
  and John Laing Infrastructure Fund Ltd reported on 20th March 2017
  "Divestment of interests in two projects for £43.4m, representing a c.36% uplift on the carrying value, and resulting in an aggregate realised IRR of c.16%."

  Following the referendum in the UK one of the key NAV valuation inputs, the implied discount rates, were re-rated upwards by up to 0.125% as Gilt yields fell. Despite this rise the discount rates applied to the long dated cash flows, which contribute to the NAV calculation of each portfolio, remain in a range between 7.5% and 9%. The conclusion is that NAVs are conspicuously conservative and premiums are a misleading measure of the value of these companies.

Sector Premiums

	Price	NAV	Premiums
Bluefield Solar Income Fund Ltd	111.25	105.7	5.25%
GCP Student Living PLC	150	136.74	9.70%
Foresight Solar Fund Limited	107.5	105.6	1.80%
GCP Asset Backed Income Fund Limited	108.25	100.01	8.24%
GCP Infrastructure Investments	128.8	110.8	16.25%
HICL Infrastructure Fund Limited	169	147.4	14.65%
John Laing Environmental Assets Group Limited	109	100	9.00%
John Laing Infrastructure Fund	133.9	116.72	14.72%
Medicx Fund Ltd	89	72.4	22.93%
NextEnergy Solar Fund Limited	110.5	102.6	7.70%
SQN Asset Finance Income Fund Limited	114	99.02	15.13%
Target Healthcare REIT Limited	114.25	101.8	12.23%
Renewables Infrastructure Group Limited	107.5	100.1	7.39%
Sequoia Economic Infrastructure Income Fund Ltd	110.25	102.88	7.16%
Greencoat UK WIND PLC	118.3	108.6	8.93%
		Average	**10.74%**
		Portfolio Weighted Average	**7.94%**

Price execution on capital raises

The VT UK Infrastructure Income Fund is designed and managed to deliver capital preservation and income and turnover is kept to a minimum. Many of the Companies in the sector have grown by issuing new equity at a discount to the prevailing price and the Fund has participated whenever the opportunity has arisen to add holdings at an advantageous price. Since inception, the Fund added to existing positions this way on over 25 occasions saving investors a combined 68.5 bps.

Trade Date	Stock	Price pre-announcement	Price Paid	Saving (£)	Saving (%)	Savings: bps vs closing price pre announcement	NAV on Trade Date	Premium
8th Feb 2016	DIGS	£1.3825	£1.3500	£0.0325	2.35%	3.1	138	-2.17%
13th May 2016	UKWG	£1.0975	£1.0500	£0.0475	4.33%	1.7	102.94	2.00%
17th May 2016	TRIG	£1.0390	£1.0100	£0.0290	2.79%	1.8	96.79	4.35%
20th May 2016	DIGS	£1.3650	£1.3610	£0.0040	0.29%	0.1	134.06	1.52%
26th May 2016	PRJC	£1.0000	£1.0000	£0.0000	0.00%	0.0	100	0.00%
27th May 2016	JLEN	£1.0138	£0.9775	£0.0362	3.58%	1.9	95.19	2.69%
8th July 2016	GCPI	£1.1900	£1.1650	£0.0250	2.10%	3.4	106.66	9.23%
22nd July 2016	NESF	£1.0175	£1.0040	£0.0135	1.33%	0.3	98.77	1.65%
9th Sept 2016	NESF	£1.0375	£1.0325	£0.0050	0.48%	0.2	99.07	4.22%
9th Sept 2016	FSFL	£1.0425	£1.0250	£0.0175	1.68%	1.9	99.3	3.22%
22nd Sept 2016	HICL	£1.7840	£1.7000	£0.0840	4.71%	3.1	142.2	19.55%
23rd Sept 2016	TRIG	£1.0480	£1.0100	£0.0380	3.63%	3.9	96.06	5.14%
25th Oct 2016	FSFL	£1.0500	£1.0300	£0.0200	1.90%	0.8	99.16	3.87%
7th Nov 2016	GABI	£1.0850	£1.0450	£0.0400	3.69%	4.5	99.42	5.11%
18th Nov 2016	UKWG	£1.1640	£1.1000	£0.0640	5.50%	1.9	105.72	4.05%
21st Nov 2016	NESF	£1.0575	£1.0450	£0.0125	1.18%	0.9	100.42	4.06%
29th Nov 2016	GCPI	£1.3250	£1.2350	£0.0900	6.79%	16.9	107.77	14.60%
5th Dec 2016	SEQI	£1.0775	£1.0500	£0.0275	2.55%	7.3	101.36	3.59%
7th Dec 2016	SQNc	£1.0000	£1.0000	£0.0000	0.00%	0.0	100	0.00%
16th Dec 2016	DIGS	£1.4625	£1.4000	£0.0625	4.27%	3.1	135.98	2.96%
8th Feb 2017	JLEN	£1.0650	£1.0100	£0.0550	5.16%	8.7	98.47	2.57%
22nd Feb 2017	DIGS	£1.4300	£1.4000	£0.0300	2.10%	1.1	136.74	2.38%
17th Mar 2017	HICL	£1.6620	£1.5900	£0.0720	4.33%	0.5	147.4	7.87%
27th Mar 2017	JLIF	£1.3292	£1.3300	-£0.0008	-0.06%	0.0	116.72	13.95%
29th Mar 2017	FSFL	£1.0825	£1.0775	£0.0050	0.46%	0.7	105.6	2.04%
30th Mar 2017	TRIG	£1.0650	£1.0300	£0.0350	3.29%	0.6	100.1	2.90%
							Total	68.5

Background Information to Investment Adviser Gravis Capital Partners (GCP)

GCP Advisory Limited is a wholly owned subsidiary of GCP LLP, a limited liability partnership. The lead advisers are Stephen West and Stephen Ellis. GCP was established in May 2008 as a specialist investor in infrastructure and now manages and advises over £1.8bn of assets in the UK, including the FTSE 250 company GCP Infrastructure Investments Limited, with market cap of over £900m. The company is authorised and regulated by the FCA. GCP have won numerous awards for their alternative approach to long-term, secure, income-producing investments.

Stephen West is the principal adviser to the Fund and having qualified for the Bar, spent 20 years in the City working in the Credit Markets, primarily at UBS where he was Global Head of Credit Trading, Underwriting, Sales and Research. In this role, he ran a division of 1000 people and was responsible for a trading book of over $400bn. He joined GCP in 2015 as a Partner to take on the lead adviser role of the UKIIF Fund.

Stephen Ellis is the supporting adviser to UKIIF. He spent 16 years in investment banking focussing on securitisation and tax-based financing and was head of Structured Finance at DTZ Corporate Finance from 2002 to 2008 where he specialised in the PFI, Infrastructure and Real Estate sectors. Stephen is a senior Partner of GCP and lead adviser to GCP's Infrastructure Investments Limited since its IPO in 2010.

Valu-Trac Investment Management

Valu-Trac Investment Management Limited was established as an authorised investment manager in 1989 and launched Valu-Trac Administration Services in 2010, to provide Authorised Corporate Director (ACD) and administration services to UK regulated funds and their delegated investment managers. Valu-Trac Investment Management Limited, as ACD, administers over £1.34bn of assets under management (as at 31/3/2017) and 24 staff in offices in the North of Scotland and London

Highland Capital Partners Ltd

Highland Capital Partners Limited ("Highland") was established in June 2009 and manages sales and marketing of the VT UK Infrastructure Income Fund. Highland has assisted in raising over £1.9bn since launch in 2009 identifying sources of new capital for IPOs, and further capital raising through C share offerings and Placing Programmes, UCIS Funds, UCITS funds, UK OEICs, VCTs and Private Equity. The company employs three distribution specialists with combined experience of over 50 years in the UK

Investing in UKIIF

Share Classes	Minimum		AMC & OCF	Currencies	ISINs
Clean	£1,000	Income	0.75%	£, €, $	GB00BYVB3J98
		Accumulation	0.75%	£, €, $	GB00BYVB3M28
Institutional	£5,000,000	Income	0.65%	£, €, $	GB00BYVB3Q65
		Accumulation	0.65%	£, €, $	GB00BYVB3T96

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