HARDMAN & CO.

5 May 2021

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VOLTA FINANCE LIMITED

Re-Set, Re-Fi, Re-Light my Fire

In this note, we explore how favourable market conditions mean that CLO vehicles can re-finance debt cheaply, thus enhancing the value of Volta's equity positions, which have been increased substantially in recent years. We show the impact on Volta's CLO debt portfolio and the wider loan market, and what this means for new investment returns. The key message is that the favourable conditions are expected to lift returns by 1%-1.5% p.a. for several years. Volta is benefiting from the unexpectedly low levels of defaults. Despite this favourable outlook, Volta still trades at a 15% discount to NAV, albeit down from March 2020 highs.

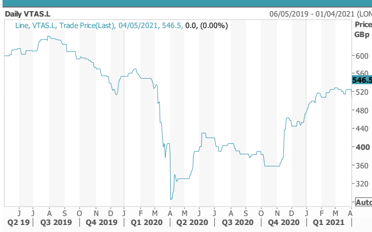
- **Re-set/Re-fi opportunity:** Volta has already seen five positions re-finance, at savings of 15bps-23bps. A further one is expected to complete in May (benefit ca.30bps), and several more in June/July. 20 positions could benefit and see the expected equity returns rise by 2% to 3%.
- **Lower-than-expected defaults:** Rating agency expectations of defaults in spring 2020 were ca.4x as high as the trailing default rate seen in March 2021. CLO vehicles have incremental rules and restrictions, meaning their defaults have typically been around half the wider market average.
- **Valuation:** Volta trades at a double discount: its share price is at a 15% discount to NAV, and we believe its mark-to-market NAV includes a further sentiment-driven discount (5%-10%) to the present value of expected cashflows. Volta targets an 8% of NAV dividend (10.2% 2022E yield on current share price).
- **Risks:** Credit risk is a key sensitivity. We examined the valuation of assets, highlighting the multiple controls to ensure its validity, in our *initiation note,* in September 2018. The NAV is exposed to sentiment towards its own and underlying markets. Volta's long $ position is only partially hedged.
- **Investment summary:** Volta is an investment for sophisticated investors, as there could be sentiment-driven share price volatility. Long-term returns have been good: ca. 8.6% p.a. returns (dividend-re-invested basis) since initiation. With above-average returns on recent re-investments, the portfolio's six-month historical cashflow yield is 16.3%, and the latest projected IRR is 13.3%. We expect 1.5x adjusted and nearly 2x statutory dividend cover in 2022.

Financial summary and valuation (Hardman & Co adjusted basis)

Year-end Jul (€m)	2016	2017	2018	2019	2020	2021E	2022E
Coupons & dividends	34.7	33.2	38.5	42.0	39.4	42.3	42.9
Operating income	36.5	35.0	37.0	41.0	31.5	44.4	43.8
Inv. manager's fees	-4.3	-4.6	-4.6	-4.4	-3.6	-3.4	-4.6
Other expenses	-0.9	-0.8	-0.9	-1.0	-1.0	-1.0	-1.0
Total comp. income	29.3	28.0	29.7	32.9	25.8	35.1	34.6
Statutory PTP	12.6	38.7	22.7	7.1	-63.0	83.6	39.4
Underlying EPS (€)	0.80	0.77	0.81	0.90	0.71	0.96	0.94
NAV per share (€)	7.92	8.36	8.36	7.94	5.69	7.46	7.92
S/P disc. to NAV*	-14%	-11%	-15%	-12%	-23%	-19%	-24%
Gearing	12%	12%	14%	12%	0%	15%	14%
Dividend (€)	0.62	0.62	0.62	0.62	0.52	0.52	0.62
Dividend yield	10.3%	10.3%	29.1%	10.3%	8.6%	8.6%	10.2%

**2016-20 actual NAV and share price, 2021-22 forecast NAV to current share price;*
Source: Hardman & Co Research

Closed-Ended Investments



Source: Refinitiv

Market data

EPIC/TKR	VTA.NA, VTA.LN VTAS LN
Price (€)	**6.04/6.03/532p**
12m High (€)	6.10/6.20/538p
12m Low (€)	3.58/3.60/327p
Shares (m)	36.6
Mkt Cap (€m)	221
2021E div. yield	8.6%
Latest NAV (€)	7.08
Discount to NAV	15%
Country of Listing	NL/UK
Market	AEX, LSE

Description

Volta is a closed-ended, limited-liability investment company that pursues a diversified investment strategy across structured finance assets (primarily Collateralised Loan Obligation, CLOs).

Company information

Independent Chairman	Paul Meader
Independent Non-Executive Directors	Graham Harrison, Stephen Le Page, Paul Varotsis
Fund Managers (AXA IM Paris)	Serge Demay, A Martin-Min, François Touati
Co. sec./ Administrator	BNP Paribas Securities Services SCA, Guernsey
Website	*www.voltafinance.com*

Key shareholders (31 Jul'20)

AXA Group	30%
BNP WM	16%
Deutsche	6%
Citibank	6%

Diary

Mid-May'21	April estimated NAV

Analyst

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Re-financing opportunity

Market conditions

With benchmark rates at/near historical lows and most CLO debt spreads back to historical lows, opportunity to re-finance at lower cost

With the strong monetary and fiscal support to the economy through COVID-19, long-term benchmark rates have fallen significantly. Most credit spreads widened initially, reflecting an increase in expected defaults, but investment grade spreads moved relatively modestly, and spreads quickly reverted to their pre-crisis levels. In terms of volumes, the impact on the CLO market, which represents more than 80% of Volta's assets, was short-lived. The US CLO market was closed for just three weeks (six weeks in Europe) at the end of March, with trading volumes and secondary market volumes at record highs in 2020. Leveraged-debt markets took more time to recover, but most senior-tranche CLO debt (i.e. the safest element) is now back to historically low spread levels. Funding costs for CLO structure are now also historically low, and this creates an opportunity to re-finance existing debt at a lower cost.

When considering re-financing of CLO, three scenarios are very common:

Simple "Re-fi"

- The structure of the CLO is unchanged, and only the most senior tranches (AAA/AA/A generally) are re-financed at a lower spread. These make up the majority of debt in most CLO structures, and so the gains from lower-cost financing can be material. Typically, the weighted average life (WAL) test of the structure is prolonged, to give more leeway to the CLO manager re-arranging the portfolio and having this better pricing locked in for an a modestly longer period.

Simple "Re-set"

- All existing debt is re-paid, and a new structure is put in place. New debt is issued, and the deal is prolonged, again locking in gains for an extended period. As the debt is re-paid, any capital gains are crystallised, to the benefit of equity holders.

Re-set with inclusion of a single B-rated tranche ("B-tranche")

- At times, when CLO debt issuance is relatively expensive, the deals may be structured without the highest-cost, B-rated tranches. The market conditions at such times also mean it is common for loan assets to be purchased at a discount. As CLO costs come down, a re-set may permit the inclusion of a higher-cost B-tranche. This increases the gearing in the structure, providing a higher arbitrage opportunity against the assets in the CLO, as well as extending its duration, locking in gains. In addition, the capital provided by the B-rated tranche can be used to upstream to the equity tranche.

Impact on Volta's CLO equity positions

Overall, two thirds of Volta's CLO equity positions expected to be Re-fi or Re-set in the coming 12 months, with typical savings in range of 20bps-50bps.

In its *interim results report* to end-January 2021, Volta highlighted the following opportunities:

- Two USD positions are amortising, and no Re-fi/Re-set can be considered.
- Two USD positions have an overall very low cost of debt.
- Nine USD positions are candidates for Re-fi/Re-set. For six of them, the gain on the overall cost of debt can be from 20bps to 40bps and, for three of them, the gain can be even higher. There is the possibility to include a B-tranche in the structure to receive an extra payment.
- 15 European positions have been issued with a B-tranche (the norm in Europe is to have a B-tranche), 10 of which are good candidates for a Re-fi or a Re-set,

with a gain on the cost of debt from 20bps to 50bps. Three European positions have, on purpose, been issued without a B-tranche. Under current conditions, a B-tranche can be issued, and the amount raised can be paid to the equity position, and the gain in terms of cost of debt can be in the area of 40bps.

If average uplift is 30bps, this would increase returns earned on equity positions by over a fifth

Most CLO structures are highly geared, and debt typically accounts for nine to ten times the amount of equity. *Ceteris paribus*, a 30bp reduction in the cost of debt thus results in an increase of 270bps to 300bps equity returns, because of this leverage. If the equity were earning 14% p.a. returns before the re-financing, it would generate 17% after the re-structuring (assuming a 10x leveraged structure after), an increase in returns of over a fifth.

Manager thinks will add 1%-1.5% p.a. to Volta's returns for several years

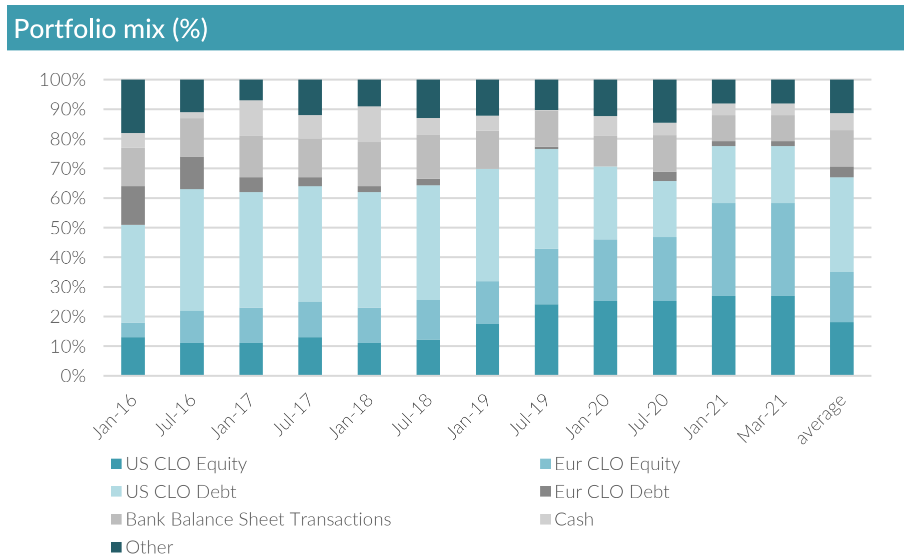
In its interim release, Volta commented that it expected such re-financing to add 1%-1.5% p.a. to the fund returns for several years to come.

Volta's move to CLO equity paid off

Portfolio has been re-positioning for optionality in equity tranches for some years

The chart below shows how, over recent years, the portfolio has been changed, with increasing holdings of CLO equity and less CLO debt. The former now makes up around 2x the proportion of the portfolio that it did in January 2019 and 3x the level five years ago. We believe some investors questioned why you would increase equity (the highest-risk tranche in the capital stack) at the same time as saying the outlook was less certain. The manager had repeatedly emphasised that the risk/return payoff was more favourable (partially reflecting the pries available at the time) and the optionality in such positions. The strong current cashflows and the potential for enhanced returns show that the strategic positioning has paid off.

Portfolio mix (%)



Source: Volta, Hardman & Co Research

Impact on Volta's CLO debt positions

Impact on existing debt positions limited

Most of the re-financing is at the option of the equity holders, and so holders of debt have little choice. In practice, the call options are typically at par and, as most of Volta's debt positions were purchased below par, there is a capital gain upside on the re-payment. One of AXA IM's core competencies is its deep understanding of the detail of the legal aspects of its investments, and so it would not purchase a position where the exercise of a call would mean it was disadvantaged.

Impact of CLO borrowers re-financing

Income that CLO structures earn is not changing materially, while expense is potentially coming down

It may be expected that the positive conditions for CLO re-financing would also mean that borrowers, whose loans are in the CLOs, would also look to lower their cost of finance. Such re-financing would see either loans being repaid or generating a lower yield, so reducing the income to the CLO. This would lower returns for equity holders in CLOs. However, it is important to differentiate between what has been happening in different parts of the market. In the mainstream market, spreads have been broadly stable, partially reflecting the expectation of some further losses. The manager highlights how the arbitrage between the asset spread and CLO debt costs is approaching two- to three-year highs, and that it is comfortably above the levels seen in 2015-17. This is consistent with prior experience, where the eventual IRR on CLO structures issued immediately after the GFC was roughly double that of the preceding years.

Impact on re-investment returns

Current income over 16% of NAV

As at 31 January 2021, the predicted IRR yield of the portfolio remained at an attractive 13.3%. In the March Factsheet, Volta highlighted that the trailing six-month cashflow represented 16.3% (annualised) of NAV, and that this could be enhanced further by i) the re-financings noted above, which could lock in multi-year gains, and ii) new CLO equity positions, which have been added recently but are yet to make their first dividend payment. Paying an 8% of NAV dividend, but receiving 16% income, would see a steady accretion to NAV without any capital gains.

Volta – projected IRR by asset class

Asset class	% gross asset value	Proj. IRR	Proj. WAL
US CLO equity	27.0%	15.8%	4.4
US CLO debt	19.3%	10.4%	3.5
Euro CLO equity	31.3%	13.6%	4.0
Euro CLO debt	1.6%	6.4%	4.5
CMV	5.2%	14.7%	4.5
Bank Balance Sheet Transactions	8.7%	9.3%	3.0
Cash corporate credit equity	1.8%	8.0%	2.0
ABS residual/lease	1.2%	10.0%	2.5
Average		13.3%	3.9

Source: Volta interim release, page 8, Hardman & Co Research

Re-investment returns may fall, but Volta's flexible mandate means it can take opportunities anywhere in the CLO chain, and there is significant upside in current portfolio

Looking forward, the continued compression of credit spreads means that the opportunity to re-invest for outsized returns is closing. Investors have been driving down the spreads for CLO debt because it is seen as an attractive option when interest rates are low and expected to be so for some time. The manager advises that there are plenty of opportunities from focusing on restructuring and enhancing existing positions, and also comments that CLO issuance is active and is expected to be so for some time. With a flexible mandate that can invest in any part of the CLO process, we note that Volta is well positioned to take opportunities wherever they may occur.

Stable portfolio from here

We understand that the manager expects CLO debt positions to generally deliver 7.5% to 8.5% coupons, making them an attractive class over the medium term. The manager also indicated that the portfolio structure was therefore likely to be stable over the forthcoming months.

Below expected default rates

Rating agency March 2020 default forecasts ca.4x actual levels seen in March 2021

We, like Volta, expect defaults to continue to materialise in 2021/2022, but the pace will be materially less than expected a year ago, and should thus be totally manageable within CLO structures. As an example, rating agencies were, at one point, forecasting 12%-14% annual default rates in 2021 for US loans. 2020 ended with just 4.6% defaults. By the end of March 2021, the trailing 12-month default rates declined again in loan markets (for the fifth consecutive month) to 3.2% and 2.0%, respectively, for US and European loans.

Current global forecasts are generally between 2% and 4% for 2021. Within its own modelling (and projected IRRs detailed below), Volta's base case is 2% p.a., except for newly issued deals, where it sets a default rate at zero for the first year. Given the business and sector mix of assets, this is believed by Volta to be consistent with market expectations for those assets.

It is important to understand why default rates have not risen as fast as was expected. This is due partially to the unprecedented government support put into the economy, but also to some structural changes in the market, most notably:

Cov-lite documentation reducing probability of default and, critically, extending time to default

- We have previously outlined why the increasing use of cov-lite documentation would mean fewer defaults and that the default events would be likely to be spread over a much longer period. We noted a range of covenant easing, with some bank contacts noting, particularly, that corporates have much more flexibility to sell assets. Butterworths' July/August *Journal of International Banking and Financial Law* noted that "in March 2020, over 86% of term loans in the S&P European Leveraged Loan Index were cov-lite, compared to just over 5% in March 2010".

Corporates been more active in seeking waivers in advance of when they need them

- The same Butterworths' article emphasises how corporates going into this crisis have been much more proactive, seeking covenant waivers in advance of needing them. It states "there were more than 145 transactions between April and mid-June 2020 in which US leveraged loan issuers are known to have obtained covenant relief, surpassing even the previous record of 25 set in 2009 as the global financial crisis unfolded." We believe this partially reflects the fact that this crisis is affecting the whole economy, not just financial institutions; however, it also shows more pro-activity by corporate treasurers to manage and protect liquidity.

Increase in PE backing provides more financially robust backers

- In several of our reports on private equity (PE) companies, we noted that PE-backed companies outperform other businesses through downturns (see, by way of example, our reports on Oakley Capital Investments, *NAV: conservative, robust and with growth upside,* published on 3 December 2020, ICGT Enterprise Trust, *Defensive growth: explaining downside resilience,* published on 8 September 2020, and Pantheon International, *Returns, resilience and responsibility,* published on 9 October 2020). This is partially because of the incremental skill and knowledge of the PE backer, but also because the PE companies have access to more committed capital. The increasing prevalence of PE-backed businesses means that an increasing number of corporate borrowers have access to such support. We note, by way of example, on slide 22 of Pantheon International's *FY'20 results presentation,* that the number of PE-backed companies in North America and Europe had risen from 9,943 in 2009 to 18,078 in 2019, while the number of public companies had fallen from 18,829 to 14,722 over the same period.

Impact is that Volta's CLO equity positions continued to pay coupons to Volta, supporting its above-average yield.

With broad sector and counterparty diversity also helping, the gently rising defaults meant none of Volta's CLO equity positions suffered any diversion of cashflow due to breaching their re-investment tests (these tests protect CLO debt holders by diverting cashflow due to the equity tranche to purchase more assets in order to increase the security protecting debt holders).

CLOs typically have around half market-wide default rates

It is also worth noting that CLO structures have historically seen loss rates around half the broader market. They are sectorally diversified but, importantly, also have incremental controls/limits in place, which restrict their holdings. This may see positions sold ahead of default, but the bottom line is that default losses are below-average.

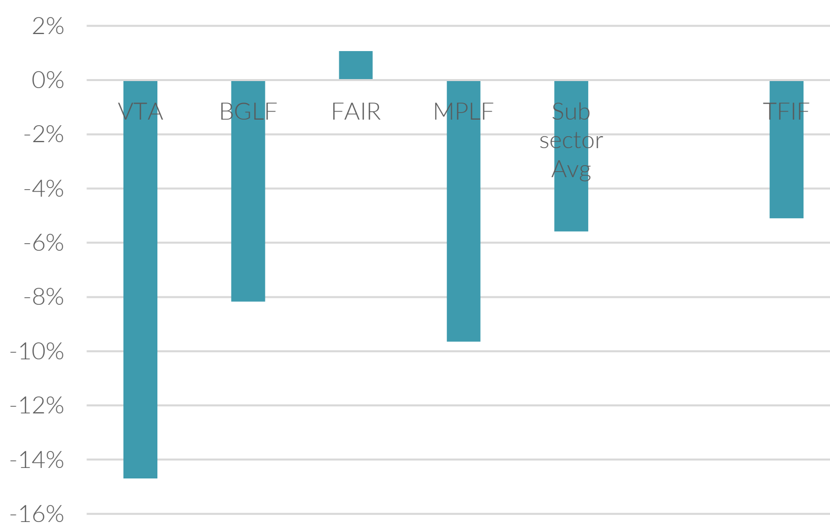
Valuation

Volta trades at a double discount: its share price is at a 15% discount to NAV, and we believe its mark-to-market NAV includes a further sentiment-driven discount (5%-10%) to the present value of expected cashflows. Volta targets an 8% of NAV dividend (10.2% 2022E yield on current share price).

Discount larger than peers on same accounting basis

Compared with its structured debt peers, on market price to NAV, Volta is trading at a discount. Given the historical performance, risk profile and portfolio mixes identified in the sections below, this relative discount appears anomalous.

Current share price discount to latest NAV for Volta and peers



Source: Hardman & Co Research, Monthly reports for Volta (VTA), TwentyFour Income Fund (TFIF), Fair Oaks Income Fund (FAIR), Blackstone/GCO Loan Financing Ltd (BGLF) and Marble Point Loan Financing (MPLF); priced 4 May 2021

Financials

Volta released its interim results to end-January 2021 in early April, and provides monthly NAV updates. We have updated our forecasts for both, including higher coupons and dividends, slightly lower gains, lower base management fees and the €5m performance fee.

Profit and loss account (statutory)									
Year-end Jul (€m)	2014	2015	2016	2017	2018	2019	2020	2021E	2022E
Coupons and dividends received	31.4	33.7	34.7	33.2	38.5	42.0	39.4	42.3	42.9
Net gains on sales	6.1	12.6	2.7	3.1	0.0	0.5	-7.0	2.5	2.5
Unrealised gains and losses	12.2	21.0	-18.5	4.7	-5.7	-18.2	-87.9	47.5	1.5
Net gain on fin. assets at FV through P/L	49.7	67.2	18.9	40.9	32.7	24.4	-55.5	92.3	46.9
Net FX	1.6	-8.2	0.3	5.6	-2.0	-11.6	-1.4	1.6	0.0
Net gain on IR derivatives	-0.3	0.0	0.0	0.4	-0.9	1.6	0.0	0.0	0.0
Interest expense on repo	0.0	-0.2	-0.9	-1.1	-1.4	-1.6	-0.8	-0.4	-1.6
Net bank int. & charges	0.0	0.0	-0.1	-0.1	-0.1	0.1	0.0	0.0	0.0
Operating income	50.9	58.8	18.2	45.7	28.4	12.8	-57.7	93.5	45.3
Inv. manager's fees	-3.6	-3.9	-4.1	-4.1	-4.2	-4.2	-3.9	-3.4	-4.6
Inv. manager's performance fees	-1.9	-5.0	0.0	-1.5	0.0	0.0	0.0	-5.3	0.0
Directors' remuneration & expenses	-0.4	-0.5	-0.6	-0.5	-0.5	-0.5	-0.5	-0.4	-0.4
Other expenses	-1.0	-1.8	-0.9	-0.8	-1.0	-1.0	-0.9	-0.9	-0.9
Total expenses	-6.9	-11.2	-5.6	-6.9	-5.7	-5.7	-5.3	-9.9	-5.8
Profit and total comp. income	44.0	47.6	12.6	38.7	22.7	7.1	-63.0	83.6	39.4
Avg. no shares for EPS calculation (m)	36.1	36.5	36.5	36.5	36.56	36.59	36.61	36.61	36.61
Statutory EPS (€)	1.22	1.31	0.34	1.06	0.62	0.19	-1.72	2.28	1.08
Total dividend (€)	0.60	0.62	0.62	0.62	0.62	0.62	0.52	0.52	0.62

Source: Volta, Hardman & Co Research

Adjusted profit and loss

To derive our adjusted profit and loss, we strip out the capital movements, including i) unrealised gains/losses, ii) FX movements, and iii) net gain of IR derivatives. We have left in realised gains, which, although volatile, have been converted into cash, and some capital gains might be expected to form part of the normal course of business. We have also backdated the current management fee structure, and adjusted it to the new level of profitability.

Hardman & Co adjusted profit and loss account (€m)									
Year-end Jul (€m)	2014	2015	2016	2017	2018	2019	2020	2021E	2022E
Coupons and dividends received	31.4	33.7	34.7	33.2	38.5	42.0	39.4	42.3	42.9
Net gains on sales	6.1	12.6	2.7	3.1	0.0	0.5	-7.0	2.5	2.5
Net gain on fin. assets at FV through P/L	37.5	46.2	37.4	36.2	38.5	42.5	32.4	44.8	45.4
Interest expense on repo	0.0	-0.2	-0.9	-1.1	-1.4	-1.6	-0.8	-0.4	-1.6
Net bank interest & charges	0.0	0.0	-0.1	-0.1	-0.1	0.1	0.0	0.0	0.0
Operating income	37.5	46.0	36.5	35.0	37.0	41.0	31.5	44.4	43.8
Inv. manager's fees	-4.1	-4.5	-4.3	-4.6	-4.6	-4.4	-3.6	-3.4	-4.6
Inv. manager's performance fees	-2.5	-3.5	-1.3	-1.2	-1.3	-2.1	-0.6	-4.6	-3.2
Directors' remuneration & expenses	-0.4	-0.5	-0.6	-0.5	-0.5	-0.5	-0.5	-0.4	-0.4
Other expenses	-1.0	-1.8	-0.9	-0.8	-0.9	-1.0	-1.0	-1.0	-1.0
Total expenses	-7.9	-10.3	-7.2	-7.0	-7.2	-8.0	-5.7	-9.4	-9.2
Profit and total comp. income	29.5	35.7	29.3	28.0	29.7	32.9	25.8	35.1	34.6
Adjusted EPS (€)	0.82	0.98	0.80	0.77	0.81	0.90	0.71	0.96	0.94
Dividend cover (x)	1.36	1.58	1.29	1.24	1.31	1.45	1.36	1.84	1.53

Source: Volta, Hardman & Co Research

Balance sheet and cashflow

Financial assets grow strongly through a combination of a strong recovery in unrealised losses and the re-introduction of conservative levels of gearing.

Balance sheet									
@ 31 Jul (€m)	2014	2015	2016	2017	2018	2019	2020	2021E	2020E
Financial assets at FV through P/L	256.3	307.3	324.1	321.3	325.7	325.5	201.7	306.6	325.5
Derivatives	0.0	0.0	1.2	0.7	1.3	0.8	2.8	2.8	2.8
Trade and other receivables	0.0	38.1	5.0	0.3	12.9	5.5	0.0	0.0	0.0
Cash and cash equivalents	19.5	0.4	10.9	37.1	20.5	14.5	9.7	9.5	7.5
Total assets	275.8	345.8	341.3	359.4	360.4	346.2	214.2	318.8	335.8
Loan financing under repos	0.0	27.3	40.3	38.1	42.7	35.9	0.0	40.0	40.0
Interest payable on loan financing	0.0	0.1	0.1	0.1	0.2	0.2	0.0	0.1	0.2
Derivatives	0.2	0.3	0.0	0.0	0.1	0.3	2.8	2.8	2.8
Trade and other payables	2.0	19.0	11.6	15.6	11.7	19.2	3.2	3.2	3.2
Total liabilities	2.1	46.6	52.0	53.8	54.7	55.7	6.0	46.1	46.2
Net assets	273.6	299.2	289.3	305.5	305.7	290.6	208.2	272.7	289.6
Period-end no. shares (m)	36.5	36.5	36.5	36.5	36.6	36.6	36.6	36.6	36.6
NAV per share (€)	7.50	8.20	7.92	8.36	8.36	7.94	5.69	7.46	7.92
Total debt to NAV	0%	9%	12%	12%	14%	12%	0%	15%	14%

Source: Volta, Hardman & Co Research

Cashflow									
Year-end Jul (€m)	2014	2015	2016	2017	2018	2019	2020	2021E	2022E
Total comprehensive income	44.0	47.6	12.6	38.7	22.7	7.1	-63.0	83.6	39.4
Net gain on financial assets at FV in P/L	-49.7	-67.2	-18.9	-40.9	-32.7	-24.4	55.5	-92.3	-46.9
Net move't in unreal. gain on reval. derivs.	0.3	0.1	-1.5	0.5	-0.5	0.7	0.6	0.3	0.3
Interest expense on repos	-1.6	0.2	0.9	1.1	1.4	1.6	0.8	0.4	1.6
FX losses on re-translation repos	0.0	-0.9	-0.3	-2.2	0.4	2.0	0.9	0.0	0.0
(Increase)/decrease in trade receivables	-1.8	0.0	0.0	-0.1	0.1	-3.2	3.2	0.0	0.0
Increase/(decrease) in trade payables	0.1	2.0	-1.5	1.6	-1.7	0.1	-0.3	0.0	0.0
Directors/other fees paid in cash	0.0	0.2	0.1	0.1	0.2	0.1	0.0	0.0	0.0
Net cash inflow/(outflow) from op. acts.	-8.6	-18.0	-8.5	-1.0	-10.3	-15.9	-2.4	-8.1	-5.6
Cashflow from investing activities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Coupons and dividends recd.	31.4	33.3	33.6	34.4	38.0	42.2	39.9	42.3	42.9
Change in margin/deriv. sett.	1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Purchase of financial assets	-71.5	-99.3	-127.0	-109.0	-138.8	-117.8	-68.1	-173.1	-133.1
Proceeds from sales of financial assets	72.2	96.9	84.9	125.5	114.2	118.2	83.0	118.0	118.0
Net cash inflow/outflow from invest. acts.	33.6	30.9	-8.5	50.9	13.4	42.7	54.8	-12.7	27.8
Cashflows from financing activities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Dividends paid	-17.0	-22.3	-22.6	-22.7	-22.7	-22.3	-19.4	-19.0	-22.6
Net sales of shares	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Proceeds from repos	0.0	28.2	13.3	0.0	4.2	-8.8	-36.8	40.0	0.0
Interest paid on repos	0.0	-0.1	-0.8	-1.1	-1.3	-1.7	-1.0	-0.4	-1.6
Net cash inflow from financing activities	-16.8	5.8	-10.2	-23.7	-19.7	-32.8	-57.2	20.5	-24.2
Net increase in cash and cash equivalents	8.2	18.7	-27.2	26.2	-16.6	-6.0	-4.8	-0.3	-2.0
Opening cash and cash equivalents	9.7	19.5	38.1	10.9	37.1	20.5	14.5	9.7	9.5
Effect of FX	1.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Closing cash and cash equivalents	19.5	38.1	10.9	37.1	20.5	14.5	9.7	9.5	7.5

Source: Volta, Hardman & Co Research

Performance fee

€5.1m performance fee incurred, as Volta's HWM reduced for dividends but, somewhat unusually, not increased by hurdle rate. Fully disclosed, but we are not sure investors and commentators will have picked up the nuance.

In 1H'21, Volta accrued a €5.1m performance fee. The policy is clearly laid out in public documents and on the website as ""*In respect of any Incentive Period, the High Water Mark is the NAV per share (net of Incentive Fees) at the end of the most recent Incentive Period in respect of which an Incentive Fee had been paid (the HWM Incentive Period), less any dividends per share which have been declared by the Company from the end of the HWM Incentive Period until the end of the Incentive Period in respect of which the High Water Mark is being calculated. In respect of the Incentive Period commencing on 1 August 2017, the High Water Mark is equal to 8.35 euros (being the NAV per share as at 31 July 2017) less any dividends per share which are declared by the Company during such Incentive Period*." However, it is unclear to us whether all investors and commentators will have picked up the nuance.

The basic principle of an absolute High Water Mark (HWM) is to make sure no performance fees are gained, as long as investors have not had at least a positive performance since the last time a performance fee was obtained. As the HWM is expressed in NAV per share, it is hence reduced by the dividend per share paid to investors to have an NAV threshold that corresponds to the basic principle indicated above. Consequently, the €8.35 original threshold was reduced by €1.76 for subsequent dividends to an effective €6.59, to determine the HWM for FY'21. The incentive fees for FY'21 thus depend on whether the annual performance for the year will be above the 8% hurdle rate (or not), and applied to the higher of the HWM (i.e. €6.59) and the end of FY'20 closing NAV (€5.73), so that it is applied to the HWM.

Board was aware and notes obverse scenarios where AXA would "miss out" on performance fees

Volta's Chair advises that, at the last review, "*a number of different configurations were reviewed and a wide range of scenarios were modelled to compare outcomes*." A scenario of a sharp fall and rapid recovery was considered, and so the performance fee outturn in 1H'21 was not a surprise to the Board. The Chair also commented that "*there are, similarly, obverse scenarios where AXA could "miss out" on a performance fee*."

An obvious example would be the bar being set higher after a period of outperformance

If the fund delivered a stellar performance in one year, it would earn the performance fee that year. However, this means that the manager then needs to earn the hurdle rate on the higher NAV. We give an example in the table below. Here, year two and three's 20% returns on opening NAV would see no performance fee earned.

Example of "missed" performance fee

Year	0	1	2	3
NAV	100	300	320	340
Performance fee due		Y	N	N
Annual return as % opening NAV		200%	20%	20%

Source: Volta interim release, page 8, Hardman & Co Research

Manager believes structure in line with market practice for comparable structure. Listed CLO very different vehicle.

In our discussions with the manager, it noted that, across AXA, there are a range of performance benchmarks with absolute HWMs, absolute and relative HWMs, IRR triggers and relative HWMs. For most hedge funds, which the manager considers to be the closest comparator to Volta, an absolute HWM reduced for capital payments was considered the standard. The manager also noted, among the closest peers, that i) FairOaks has a final IRR trigger but the legal structure is different, and so this is not an option for Volta, ii) BGLF does not have one, and iii) TORO takes a 15% performance with an absolute HWM.

Performance fee when NAV has fallen unlikely to be welcomed, but represents around three months of shareholder returns

We do not believe a €5m performance fee, when the NAV has fallen, will be welcomed by investors. To put it into perspective, it is under 2% of NAV, less than three months of the average returns earned since inception/over the past five years, and around a quarter of the dividend expected to be received by shareholders this year. We also note that the management fee is NAV-driven and was down €0.5m 1H'21 on 1H'20.

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