Lucerne Alternative Investments Fund

QUARTERLY REPORT | MARCH 2021

Lucerne
Alternative
Investments
Fund

Lucerne Alternative Investments Fund Quarterly Update

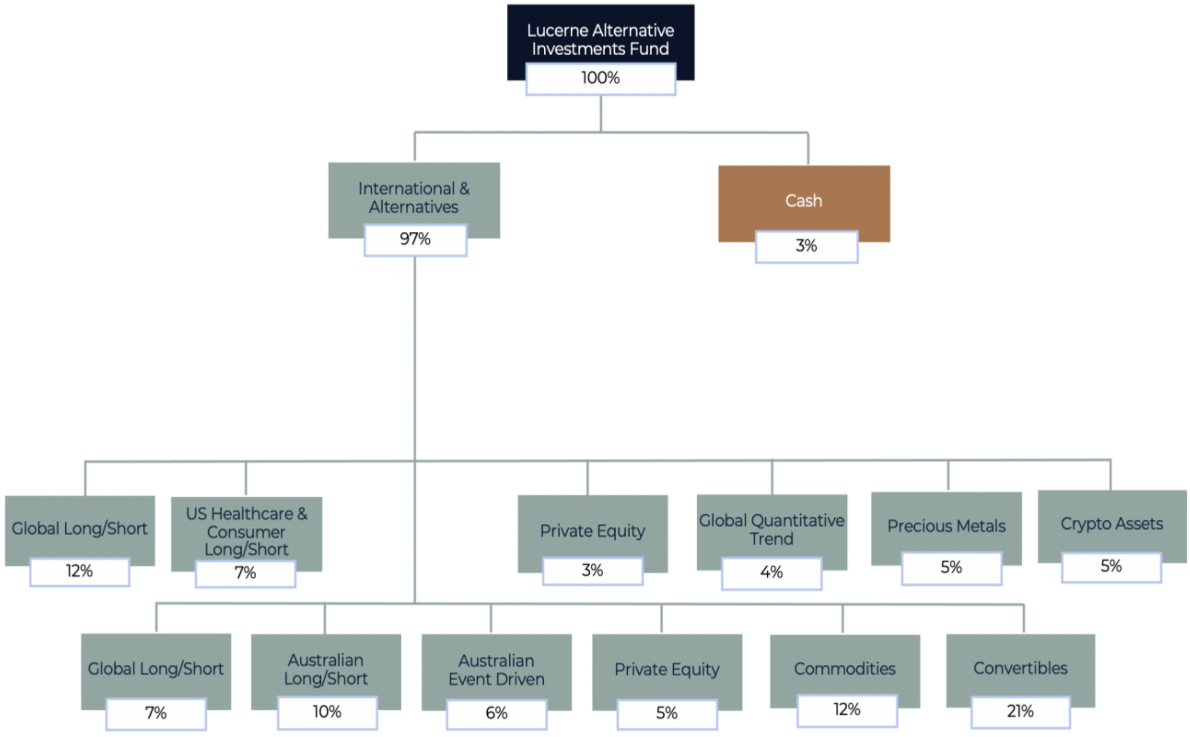
Making bold predictions about the future tends to be pointless. Of the 50 leading managers interviewed by Livewire at the end of 2019 on their 2020 outlook, understandably, not one of them flagged a pandemic and its potentially devastating effects.

Knowing we can never predict the future, we follow the strategy of actively managing a genuinely diversified portfolio of alternative investments. The portfolio's purpose is to participate in market strength, avoid market pullbacks, and ultimately deliver quality, risk-adjusted returns.

LAIF achieved a net return of 21.23% for calendar year 2020 and largely avoided the dramatic drawdowns most funds endured through the COVID crash. Importantly, LAIF's volatility was around one third of the equity market volatility over the course of the year.

Diversification is perhaps an overused term, but to illustrate the diversification we seek, LAIF is allocated across a wide range of themes that include domestic and global long/short funds, private equity, precious metals, volatility funds, event-driven strategies, commodities, convertible debt as well as a small exposure to crypto assets.

The fund has started 2021 strongly with a positive 6.2% return to end February, and March estimated to return a positive 1.9%, taking the first quarter's return to an estimated 8.1%. After a robust start to the year, we believe the fund remains well-positioned for the full spectrum of challenges that may lay ahead.



Life after COVID

This time last year, most major economies had just gone into lockdown in response to the new and poorly understood threat of COVID-19. It's truly remarkable to consider that as little as twelve months later, not only are effective vaccines available but that 806 million people, or 11.3%, of the global population, have already received their first shot, with that figure standing as high as 38% in North America.

As we have seen with concerns over the AstraZeneca vaccine in several countries causing interruptions, the global vaccine rollout is unlikely to follow a linear path and further challenges to such a massive undertaking are inevitable. However, with 38% of people in North America having received their first vaccination already, at the current rate of 1,021 vaccinations per 100,000 people per day, the other 62% could theoretically have had their first vaccination within two months.

	Countries vaccinating	Doses administered	▾ Adults with first dose	Adults with second dose	Vaccinations per day, per 100,000
World	155/195	806m	11.3%	4.2%	206.5
North America	3/3	210m	38.0%	19.8%	1,021.
European Union	27/27	97.3m	19.6%	7.7%	473.7
Rest of Europe	21/23	81.1m	18.8%	7.7%	348.0
South America	12/12	51.3m	12.6%	4.5%	431.3
South Asia	6/6	118m	10.0%	1.4%	360.0
East Asia	14/16	198m	8.5%	2.9%	236.8
MENA	18/21	39.1m	7.7%	4.9%	122.4
Oceania	4/10	1.27m	4.2%	0.07%	156.8
Central America	17/20	2.94m	3.9%	0.9%	46.8
Central Asia	6/8	2.13m	1.0%	0.1%	27.3
Sub-Saharan Africa	27/49	4.5m	0.9%	0.01%	11.6

Source: [Economist] (as of 14/04/21)

This simplistic analysis overlooks the complex supply-chain challenges, the fact that some people will always refuse the vaccination and the risks posed by new variants such as Brazil's P1. However, the data brings into view the fact that baseline immunity levels could be just months away in the US.

The situation is not quite as positive in the European Union, with less progress so far, and several countries back in lockdown. All the same, the rollout is accelerating, and based on the data above, the whole of the EU would in theory have had a first vaccination by November.

Echoing the US vaccination rollout data above, the chart below from Payden and Rygel, a US-based asset manager with $135 billion under management, shows how near the US, and other major economies are to closing the output gap, i.e.: getting the economy back to where it was pre-COVID. By their assessment, the US economy will have soon made a full recovery and tipped into the black.

Per cent change from Pre-Pandemic Projections for 2021 Q4 Economic Growth

Source: Payden and Rygel, data from OECD Economic Outlook database and calculations:

This remarkable milestone draws close while the Fed fund rate remains at a record low, QE continues, Biden's $1.9 trillion Economic Stimulus Plan is being deployed, and an additional $3 trillion infrastructure package is being finalised. Paraphrasing the late Senator Everett McKinley Dirksen, 'a trillion here and a trillion there, and pretty soon you're talking real money'.

So, with the US suddenly starting to envisage 'life after COVID', while monetary settings and fiscal stimulus are at historically supportive levels, for the first time in a generation, the market is factoring in a real risk of inflation returning.

In a Bloomberg interview, Bridgewater Associates' founder, Ray Dalio said: *"Think of the economy as being like an individual and their pulse is dropping. When the pulse is dropping, the doctors come running in with the stimulant and they inject the stimulant. Now that the economy is rebounding, inflation pressures are rebounding."*

Market Movements

In a recent note from specialist precious metals manager Baker Steel, the authors flagged inflationary risk as a significant potential catalyst for gold, saying that:

“Gold has historically thrived as an inflation hedge during periods of rising prices. While inflation has remained low for most major economies over the past decade, the global economic response to the COVID-19 crisis, driven by historic levels of economic stimulus, appears likely to unleash inflationary pressures in the months and years ahead. Money printing, heightened government spending on infrastructure and the “green deal” fuelled by debt, increased bank lending and pent-up consumer demand, alongside supply-side factors including “reshoring” and the impact of lengthy economic shutdowns, indicate a rise in consumer prices is likely”.

Baker Steel believes that gold’s ~19% fall between August 2020 and March 2021 as being completely in-line with previous mid-cycle pullbacks and argue that as well as the inflation risk, low and negative real interest rates (nominal rates minus inflation), the rapid jumps in M2 money supply and debt, and the persistent geopolitical tension are all supportive of a continued bull market in gold.

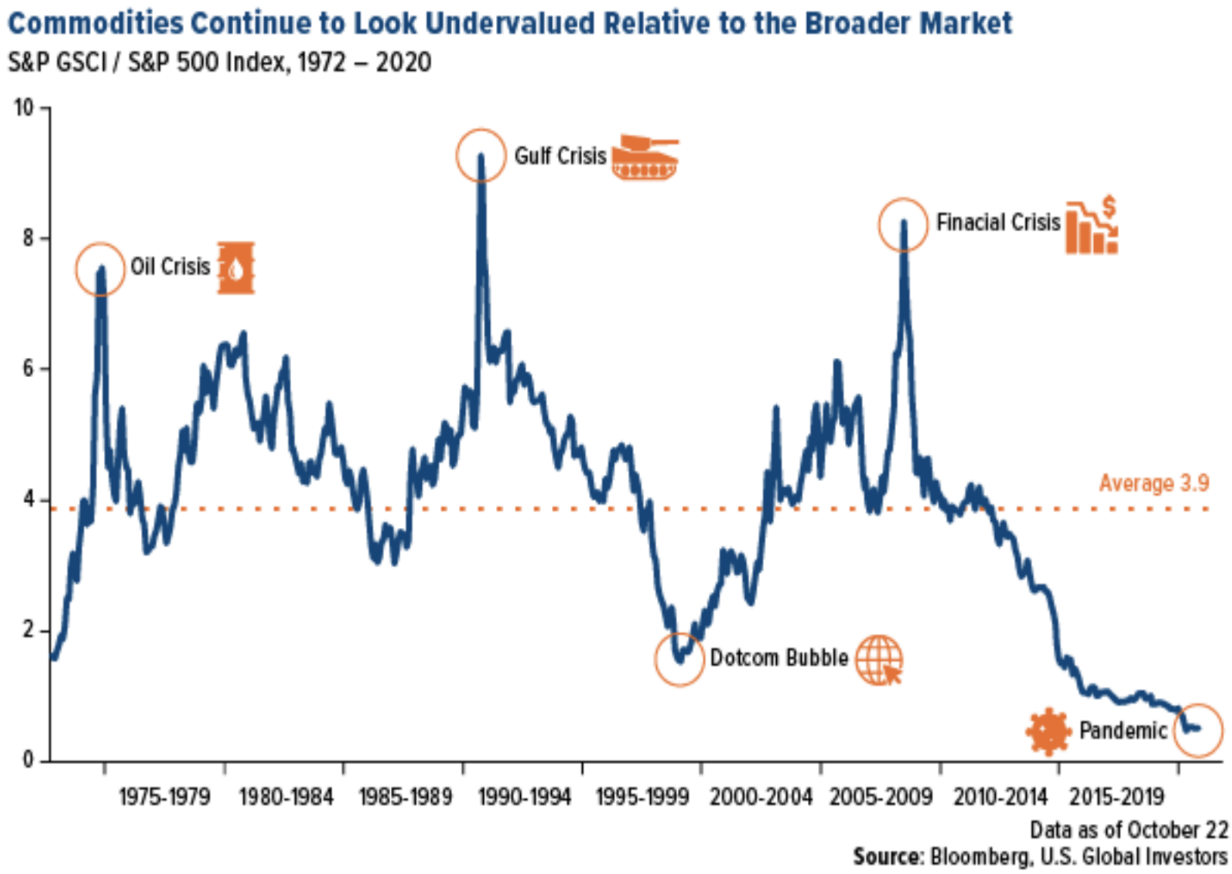
A mid-cycle pullback - Gold’s recent sell-off is consistent with past cycles

Source: Bloomberg, Baker Steel Capital Managers LLP. Data at 15 March 2021.

LAIF has an allocation to Baker Steel, and while this mid-cycle correction has impacted the performance of Baker Steel’s fund, the manager argues that the gold industry is in the healthiest shape it has been in for a long time and is offering ‘historic levels of fundamental undervaluation’ that are setting gold equities up for a re-rating by the market.

As well as gold, commodities more broadly are beneficiaries of inflation. During March, Sam Berridge from Perennial’s Global Resources Trust presented to Lucerne’s investors which you can watch here or read here if you missed it. LAIF also has exposure to Perennial GRT, which has now nearly doubled in its first year since inception and has been a strong contributor to LAIF’s performance.

Sam laid out the case for commodities at the start of his presentation, pointing out that benchmarking commodities to equities, they are in the very early stages of coming off a nadir in their cycle, and thus have the potential to significantly outperform relative to equities over the long-term.

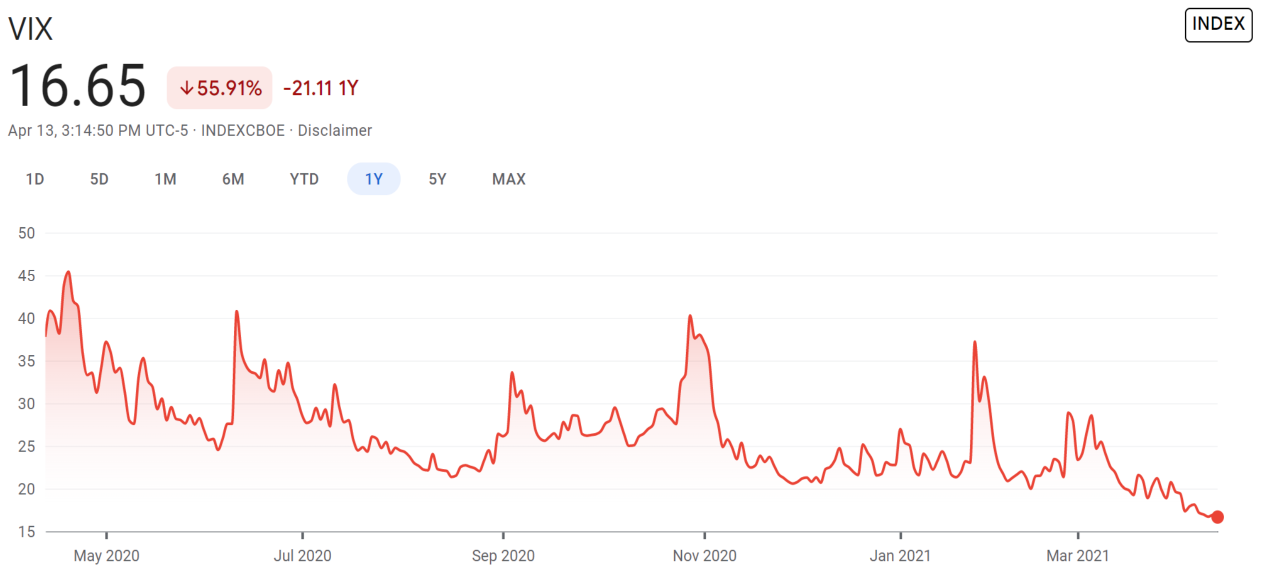


One commodity theme Sam focused on and is exposed to in his fund is the electric vehicle theme, and to demonstrate the potential scale of it, pointed out that consultant Wood Mackenize estimates that roughly $1 trillion of new mine investment will be required to meet their forecast demand for Electric vehicles by 2035.

So, while commodities look historically cheap against equities, there are obvious long-term drivers of demand coming into the market to support higher commodity prices, as well as the prospect of an inflationary tailwind.

Volatility is low but don’t get complacent

The chart overleaf is the CBOE Volatility Price Index (also known as VIX), where the intermittent spikes represent outbursts of market fear while the lower levels are associated with positive sentiment.



The VIX is presently at a long-term low and so we would consider it prudent to be prepared for the next inevitable phase of uncertainty. Volatility, or risk, is elevated at these times and we are conscious that a spike is possible without even knowing the catalyst. LAIF is positioned to withstand these periods of volatility in most market events given its unique investment strategy and weighting to asset classes.

The Investment Committee continues to discuss what impact an unexpected event could have on markets, inflation and naturally the Fear Index (VIX) and how this transfers into asset prices. We are positioning investments to prepare for such events, especially as momentum can deliver both positive and negative outcomes.

One positive outcome worth noting is the strong performance of the crypto assets fund that LAIF added a small exposure to last year. Given the resultant increase in relative weighting within the portfolio since the investment and the high volatility of the sector, which is currently being demonstrated, the Investment Committee made the decision to halve the fund's position sizing late in March to manage risk. We note at the time of writing this piece (mid-April), crypto valuations have contracted.

The Investment Committee continues to monitor asset allocation and fund sizing to introduce new opportunities, lock-in resulting performance and manage volatility, with the aim of continuing to deliver quality risk-adjusted returns for our investors.

If you, or someone you know, would like to talk with us, please do not hesitate to contact us on laif@lucernepartners.com to arrange a call. Alternatively, it is now possible to invest directly by clicking here.

--

The Lucerne Alternative Investments Fund

April 2021

Disclaimer

Summary of information: This presentation contains general information only and should not be considered to be comprehensive or purport to comprise all the information that an investor should consider when making an investment decision. This presentation is not a prospectus, disclosure document, product disclosure statement or other offering document under Australian law or under any other law. The information in this presentation remains subject to change without notice. Lucerne Investment Partners is not responsible for providing updated information and assumes no responsibility to do so.

Not financial product advice: This financial information provided in this presentation is for information purposes only. The information contained in this presentation is not a financial product, investment advice or a recommendation to acquire securities and has been prepared without taking into account the objectives, financial situation or needs of any person or entity. Before making an investment decision prospective investors should consider the appropriateness of the information having regard to their own objectives, financial situation and needs, and seek legal, taxation and financial advice appropriate to their jurisdiction and circumstances.

No liability: The information contained in this presentation has been compiled in good faith using sources believed to be reliable. However, Lucerne Investment Partners and its affiliates and each of their respective directors, agents, officers, employees and advisors expressly disclaim, to the maximum extent permitted by the law, all liabilities (however caused, including negligence) in respect of, make no representations regarding, and take no responsibility for, any part of this presentation and make no representation or warranty as to the currency, accuracy, reliability or completeness of any information, statements, opinions, conclusions or representations contained in this presentation.

Existing relationship: Lucerne Investment Partners and its affiliates may have an investment banking or other relationship with the companies that are the subject of this presentation and may trade in any of the securities mentioned in this presentation either for their own account or the accounts of their clients. Lucerne Investment Partners and its affiliates therefore may at any time have a long or short position in any such securities, related securities or in options, futures or other derivative instruments based on those securities.

Future performance: This presentation contains certain forward-looking statements and opinions. The forward-looking statements, opinions and estimates provided in this presentation are based on assumptions and contingencies which are subject to change without notice, as are statements about market and industry trends, which are based on interpretations of current market conditions. Forward-looking statements, including projections, forecasts and estimates, are provided as a general guide only and should not be relied on as an indication or guarantee of future performance and involve known and unknown risks, uncertainties and other factors. Past performance is not necessarily a guide to future performance and no representation or warranty is made as to the likelihood of achievement or reasonableness of any forward-looking statements or other forecast.

Not an offer: This presentation is not, and should not be considered as, an offer or solicitation to buy or sell securities or any other financial products. Neither this document nor any of its contents will form the basis of any contract or commitment to act as a securities broker or dealer in any jurisdiction by any person or company that is not legally permitted to carry on the business of a securities broker or dealer in that jurisdiction.

This presentation must not be disclosed to any other party and does not carry any right of publication. Neither this presentation nor any of its contents may be reproduced or used for any other purpose without the prior written consent of Lucerne Investment Partners.

Monetary values: Unless otherwise stated, all dollar values are in Australian dollars (AUD$).

Confidential: This document contains information that is strictly confidential. You must not directly or indirectly disclose to any person or copy, use, publish or record in any form any part of this document.

Lucerne Services Pty Ltd AFSL 481217

Lucerne Alternative Investments Fund

This information has been prepared by Lucerne Australia Pty Ltd ACN 609 346 581 a Corporate Authorised Representative of AFSL number 481 217 and issued by The Trust Company (RE Services) Limited ACN 003 278 831 as responsible entity and the issuer of units in the Lucerne Alternative Investments Fund. It is general information only and is not intended to provide you with financial advice and has been prepared without taking into account your objectives, financial situation or needs. You should consider the product disclosure statement, available by calling 03 8560 1440 or visiting our website www.lucernepartners.com, prior to making any investment decisions. If you require financial advice that takes into account your personal objectives, financial situation or needs, you should consult your licensed or authorised financial adviser. To the extent permitted by law, no liability is accepted for any loss or damage as a result of any reliance on this information.

No company in the Perpetual Group (Perpetual Limited ABN 86 000 431 827 and its subsidiaries) guarantees the performance of any fund or the return of an investor's capital.

Total returns shown for the Lucerne Alternative Investments Fund have been calculated using exit prices after taking into account all of Perpetual's ongoing fees and assuming reinvestment of distributions. No allowance has been made for taxation. Past performance is not indicative of future performance.

LEVEL 4, 45 WANGARATTA ST, RICHMOND, VIC 3121

+61 3 8560 1440

LAIF.COM.AU

LINKEDIN