Lucerne Alternative Investments Fund

Quarterly Report | June 2022

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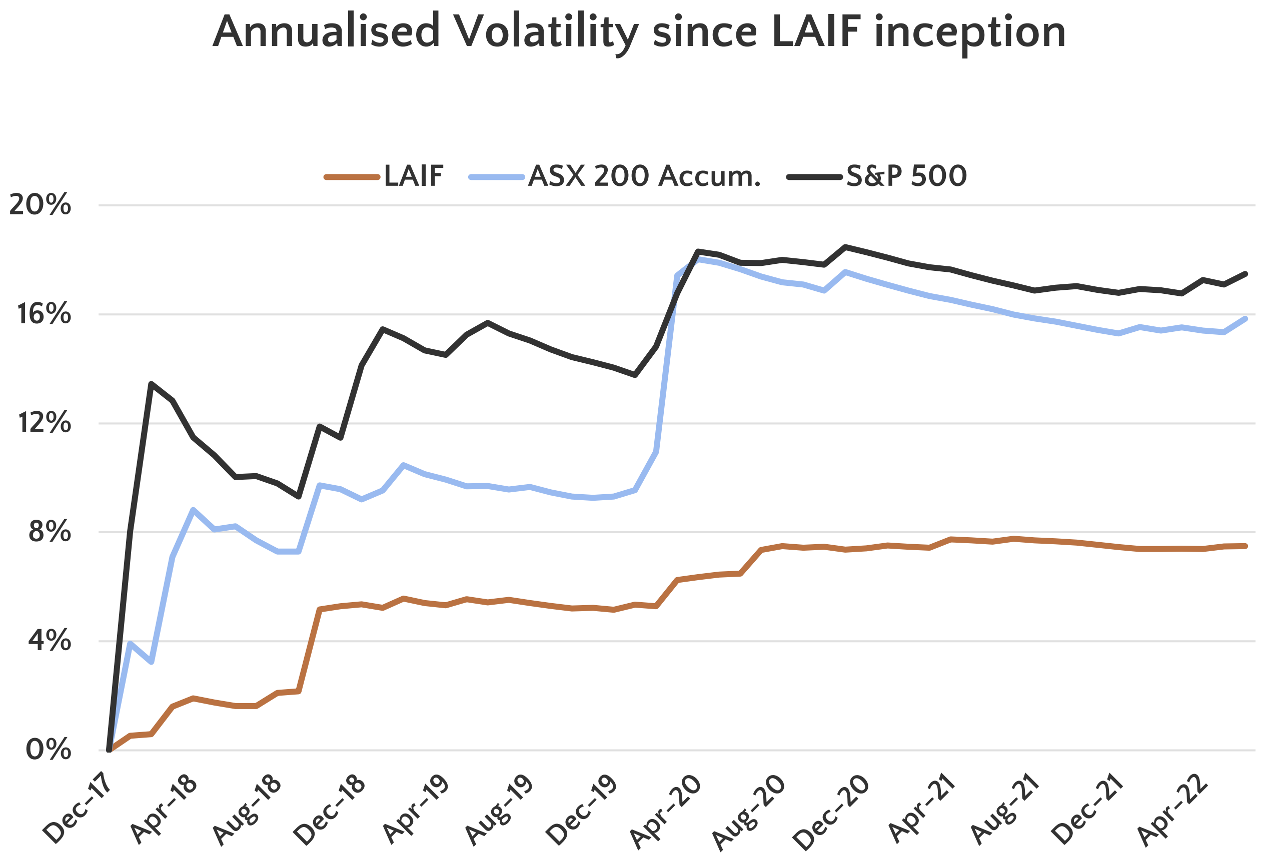
Fund

June 2022 Quarterly Report

The Lucerne Alternative Investments Fund (LAIF) returned -1.59% for the month of June bringing the quarterly performance to -1.01%. This is another good result compared to major indices around the world that entered bear market territory with drawdowns exceeding 20%. This highlights the benefits of allocating to a well managed diversified alternatives fund of funds.

The Fund continues to meet its return objective of 6% or more above the RBA cash rate after fees per annum (over a cycle), with much lower volatility than equity markets (see below).



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It has been an eventful period economically and geopolitically.

- In March, the US Federal Reserve raised the cash rate as expected by the market. For the quarter, the cash rate has increased by 150 basis points, the fastest rate hike in history.
- The RBA followed as local inflation continued to soar with rate increases in May and June of 25 and 50 basis points respectively.
- Russia's invasion of Ukraine continues to disrupt global supply chains, creating food shortages for many countries.
- Disappointingly this conflict has provided an opportunity for tensions to heat up between China and the US over Taiwan. The probability of another serious geopolitical event is gathering intensity.
- Inflation figures around the world accelerated to numbers not seen in 30-40 years.
- Crypto markets had a meltdown in May. The de-pegging of the stable coin 'Terra' to the USD saw aggressive sell downs across crypto counters.
- The Chinese property debt bubble is still ongoing with the government now stepping in and will assist the developers to complete unfinished projects.
- Supply chain disruptions are improving but the ongoing rolling lockdowns due to covid outbreaks in China are still causing supply issues.

We expect markets to remain volatile as several of these themes playout.

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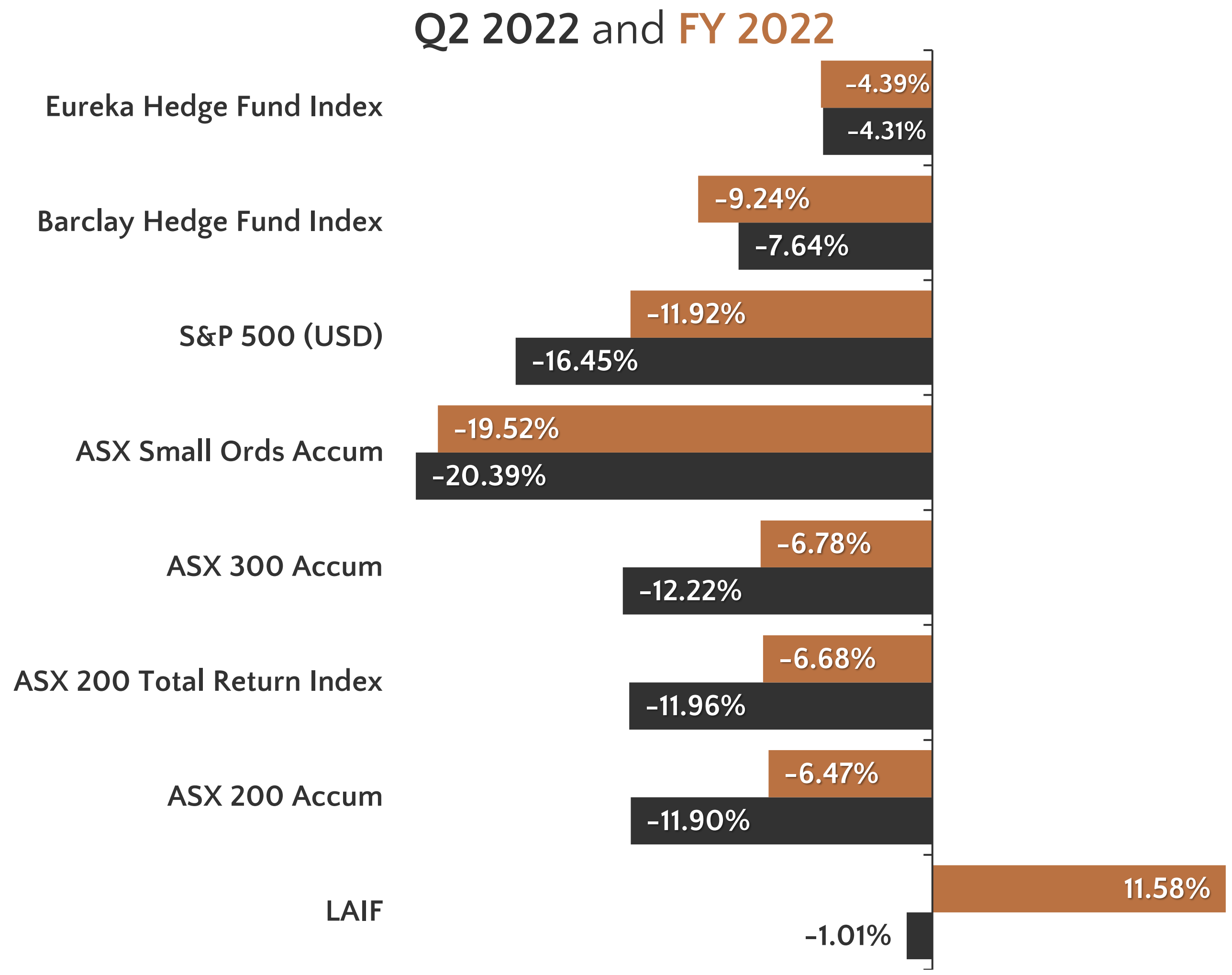

In April markets were caught off guard with the speed and magnitude of interest rate hikes and the realisation of supply chain uncertainties due to China's Zero-Covid lockdowns. Iinflation, stagflation, economic slowdown, earnings downgrades, and interest rate rises were in full force and playing a crucial role in the market pull back. The collapse of the crypto stable coins added to the market's panic selling sentiment.

The sky fell on the crypto market in early May as the stable coin 'Terra' had a free fall which caused a broad-based collapse of the asset class. Prior to the fall, Terra ranked in the top 10 crypto coins, with a market value of over US$18.7 billion and is now virtually worthless. Bitcoin, the most popular crypto currency is down a massive 70% since its peak in 2021. Wild movements like this are not uncommon this reveals the fragility of the crypto ecosystem.

Stablecoins were a subset of the crypto ecosystem designed to be immune from volatility as it was backed by collateral of real value. Terra however determined its value through a complex algorithm which depended on a sister coin called 'Luna'. The value of Terra is automatically rebalanced through the operation of its protocol by either the burning (decrease in supply) or minting (increase in supply) of its collateral coin, Luna. Basically, attempting to maintain parity through a process of arbitrage.

This process broke down in May, when investors lost conviction in the ability of Terra and Luna to produce a yield on their investments. Bitcoin lost its ground around the same time triggering a spiraling selloff in Terra which was the collateral holding the coin's real value.

For the quarter, the Lucerne Alternative Investments Fund was down 1.01%. While Q2 was not a positive quarter, LAIF is up 1.60% since 1 January which is a strong result given the turmoil in global markets. The fund is up 11.58% for the financial year ending 30 June outperforming the ASX 200 Accumulation index by 18.04%. We are pleased to note LAIF's Annualised Volatility in the same period was 60% lower than the ASX 200 Accumulation index.

Volatility

As mentioned in the opening remarks the LAIF IC is cognisant that there are many market forces that will play out over the next 6, 12 and 18 months. We are entering a period of monetary tightening to attempt to prevent inflation getting away from central banks. There will no longer be easy money to bid up asset prices across the board to achieve price growth and investment performance. Therefore, the set and forget strategy that has worked over the past ten years (for example via ETF's and index tracking long only fund managers) will most likely not be as fruitful over the next ten years. Thus, an active portfolio of diversified strategies which have low correlations to equities markets and different return profiles should outperform over this period.

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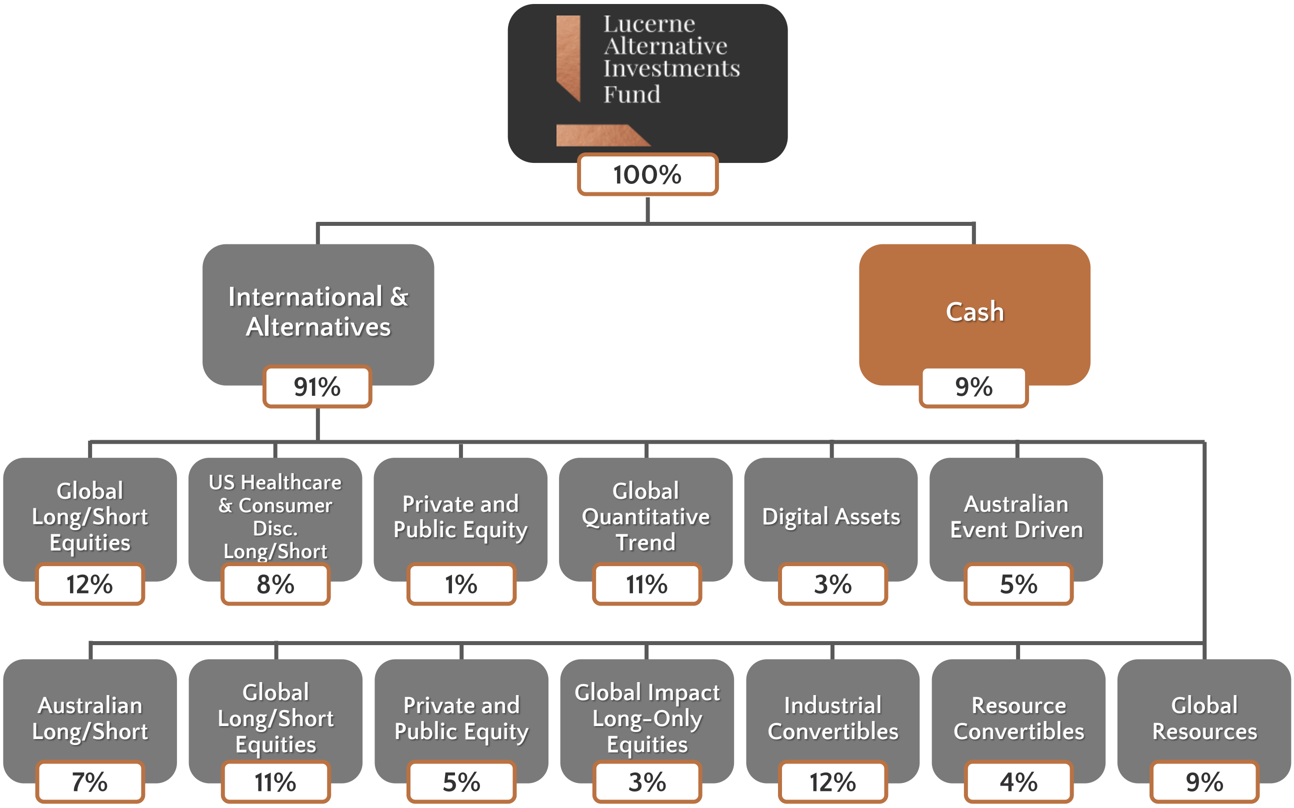
Portfolio Movements

Capital preservation and reducing correlation was front of mind over the last quarter. Thus, the Investment Committee increased exposure to resources, and digital assets and reduced exposures in precious metals. It is more important than ever to diversify alpha streams as markets try to navigate the ongoing political and macroeconomic conditions.



If you, or someone you know, would like to talk with us, please do not hesitate to contact us at laif@lucernepartners.com to arrange a call. Thank you for your interest in LAIF, and we wish you safe investing for the quarter ahead.

The Lucerne Alternative Investments Fund
Investment Committee
August 2022

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Lucerne Services Pty Ltd AFSL 481217

Lucerne Alternative Investments Fund

laif.com.au

PDS & TMD

Level 4, 45 Wangaratta Street,
Richmond 3121

+61 3 8560 1440
laif@lucernepartners.com