Lucerne Alternative Investments Fund

QUARTERLY REPORT | MARCH 2022

Lucerne
Alternative
Investments
Fund

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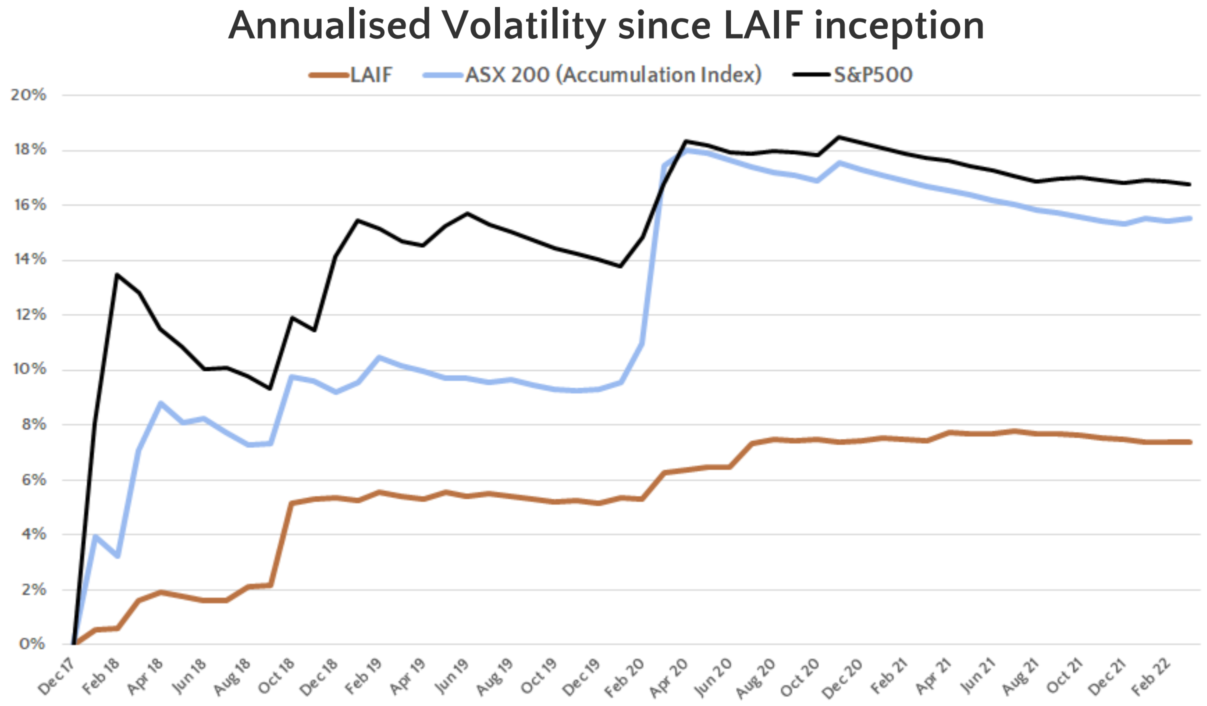
March 2022 Quarterly Report

The Lucerne Alternative Investments Fund (LAIF) is pleased to report another strong quarterly result, posting its eight consecutive positive quarter. The fund returned 3.12% for the month of March bringing the quarterly performance to positive 2.64%, despite major indices around the world detracting or remaining flat for this period. This highlights the benefits in allocating to a diversified alternatives multi strategy fund of funds.

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



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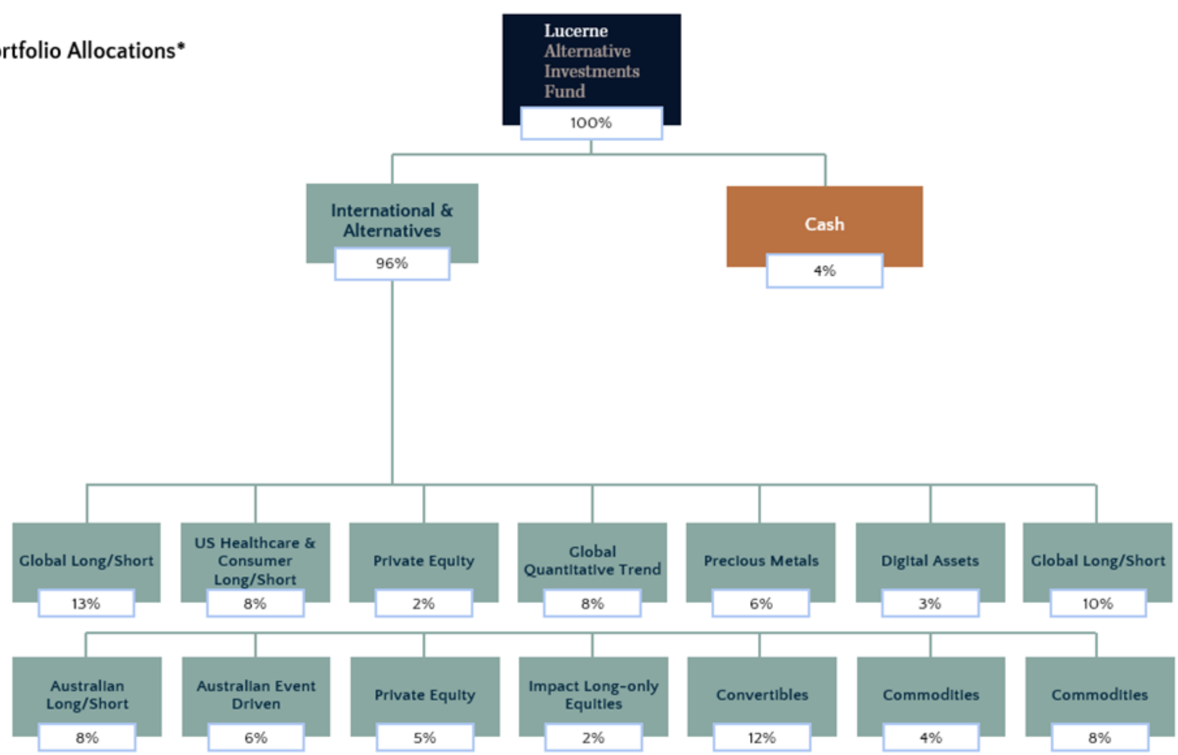
It has been an eventful period economically and geopolitically.

- In January, markets came to terms with the US Federal Reserve raising rates at a faster pace than first thought.
- Whilst the RBA remained complacent and unwilling to begin tightening monetary policy (until the May meeting).
- Unfortunately Russia made good on its threat to invade Ukraine on the 24th of February 2022, marking a large scale escalation in Russian-Ukrainian tensions.
- The Australian Federal Budget was released at the end of March and was deemed to be a crowd pleasing budget as we near a federal election.
- The Chinese property debt bubble is still ongoing with no resolution in sight.

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

Portfolio Allocations*



*Estimate only. Figures subject to rounding. Please note portfolio allocations are modified regularly.

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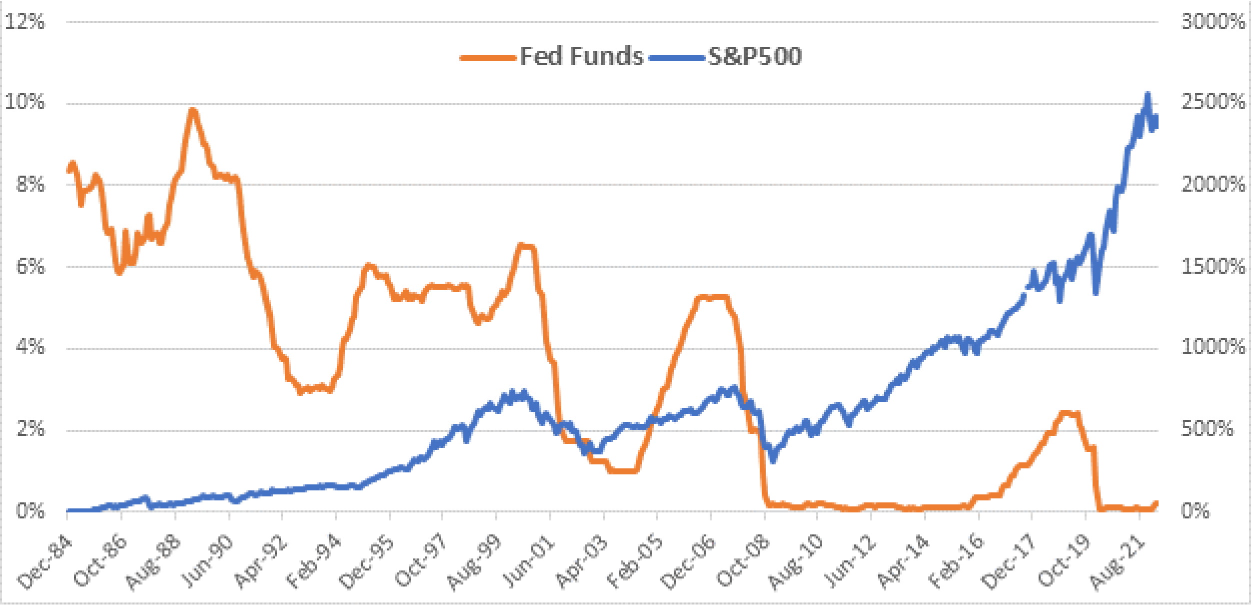
Monetary Tightening Spooks the Market in January

The month of January was a volatile one for equity investors. The S&P500 closed down 5.3%, the Nasdaq declined 9.49% and the ASX200 had a drawdown of 6.4%. This was partly due to the US Federal Reserve indicating that it will start raising rates in March to combat high inflation. This would be the first rate hike in 3 years. This was confirmed in March as the Federal Reserve increased interest rates by 0.25%. Markets have priced in five to six rate hikes in 2022. Historically, as interest rates have been declining, particularly since the GFC, equity markets have been in a Goldilocks environment where investors are happy to pay inflated prices for growth and technology stocks as displayed in the chart below.

In recent history the only time we have seen the Federal Reserve begin raising rates was in the December quarter 2018 which saw the S&P500 decline 14.8%. Central banks now have no choice with the threat of high sustained inflation but to remove the ”Punchbowl” causing growth assets to decline as was seen in January this year. This also has a negative impact on bonds, as the market prices of existing bonds immediately decline as new bonds are offering investors higher interest rate returns. The Reserve Bank of Australia (“RBA”) has now followed suit raising rates by 25 basis points to an RBA cash rate of 35 basis points. The 4 big banks in Australia have passed on these rate rises in full to borrowers, however investors are yet to see a meaningful benefit.



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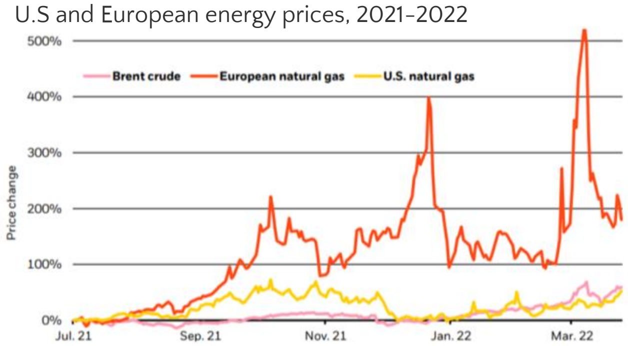
Russia at it again!

Since the collapse of the Soviet Union, the National Atlantic Treaty Organisation ("NATO") has begun pushing eastward accepting the majority of the eastern European nations. NATO has intended to invite Ukraine into NATO since 2008. Russia and therefore Putin believes NATO's expansion is a great threat to Russia and the prospect of Ukraine joining would be a hostile act. This saw Russia begin a full-scale invasion of Ukraine with the largest mobilisation of forces Europe has seen since 1945. This came after months of speculation where Russia had amassed 150,000 troops encircling the Ukraine border on three sides.

In response, major countries around the world have summoned large scale economic sanctions against Russia. This saw food commodity prices soaring to the highest levels ever recorded as Russia and Ukraine account for 30% of global wheat exports and 20% of maize exports over the last 3 years. The west is attempting to reduce its reliance on Russian Oil and Gas. However, Russia is the European Union's largest supplier of oil, coal and gas (27%, 47% and 41% of imports, respectively). This will result in higher inflation, slower growth, and increase demand for non-Russian fossils fuels in the short term. However, it is likely to expedite the transition by major European economies to other energy sources, in particular renewable energy.

Energy supply shock

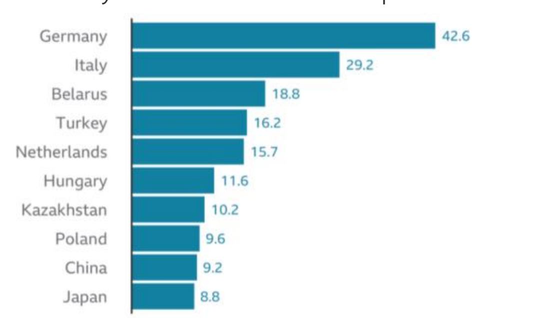
U.S and European energy prices, 2021-2022



Sources: BlackRock Investment Institute, with data from Refinitiv Datastream, March 2022. The lines show the changes in price of different commodities since July 1, 2021. European natural gas price based on European Energy Derivatives Exchange futures, U.S. based on MYM-Henry Hub Gas futures price. Oil price based on ICE-Brent crude futures.

Russia's gas exports

Countries by billion of cubic metres imported from Russia



Source: IEA, Data for 2020 BBC

LAIF did not have any direct exposure to Russia.

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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.

Portfolio Movements

Capital preservation and reducing correlation was front of mind over the last quarter. Thus, the Investment Committee increased exposure to gold, impact investing and systematic trend following. 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
April 2021

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