

March 2022 // Issue 14

# IN THE FRAME

## PEACEKEEPING (INVASION)

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### FUND PERFORMANCE

How our strategies performed in February

### COMMODITY MAYHEM

How the Russian invasion impacts commodity markets

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# WHAT I SAW FEBRUARY 2022

WRITTEN BY HUE FRAME

*In this issue of 'What I saw', Hue covers the recent invasion of Ukraine, the wild price action seen in commodity markets and how our strategies performed in February.*

Coming into the month of February, most market participants had hoped for a month with less volatility, however, what participants got was another wild period for global investment markets. We labeled January as the month of rotation, as investors moved money out of high-growth tech stocks and into investments that would benefit from a rising interest rate environment.

February saw Russia invade Ukraine, which accentuated the volatility seen in January. In an environment that was already concerned with inflationary risk, the invasion of Ukraine, and the subsequently imposed sanctions on Russia, caused Oil, Wheat, Corn, and Natural Gas to rise by +8.70%, +21.94%, +11.43%, and +13.33% respectively, due to Russia being such a large producer of these commodities.

Gold and Silver rose by +6.22% and +8.88% respectively, as investors rushed to physical safe-havens. The S&P 500, Nasdaq, and Dow Jones Industrial Average all declined by over -3.00%. The S&P/ASX 200 outperformed relatively to its peers, it rose +1.11%.

## Russian invasion

On the 21st of February, Russian officials recognised two self-proclaimed states in the Donbas and sent troops to the territories. Three days later, Russia launched a full-scale peacekeeping mission (invasion), Putin claimed the intention was to 'denazify' Ukraine. This move sent shock waves through global markets and has far-reaching implications on global trade, supply chains, and commodity prices.

## Interest rate decision

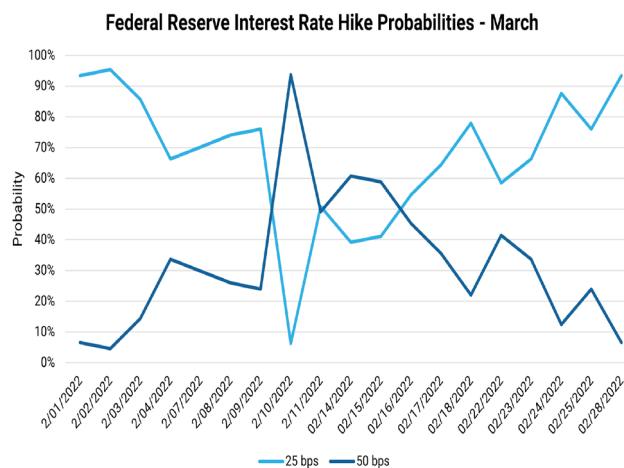
On the 10th of February, expectations for a 50bps increase of the US Federal Funds Rate were 93.8%. At the conclusion of the month, expectations had dropped to 8.5%. Interestingly, expectations at the start of February were high because of the concerns of out-of-control inflation. In our view, the risk of further spikes in inflation had increased due to further supply chain disruptions and a reduction in global supply



**HUE FRAME**

Managing Director & Portfolio Manager

due to Russian sanctions. It is worth monitoring how the next round of inflation data looks considering the aforementioned price rises of these key production inputs.



## Portfolio performance

During February, both strategies had adapted to the environment of increased volatility in January which meant we were on the front foot. The Long Short Australian Equity strategy rose by +3.16%, while our global macro strategy dropped -0.88%.

The Frame Long Short Australian Equity Fund (FLSAEF) rose by +3.16%. Following on from last month, the systematic risk management of the strategy kicked into gear, which increased our cash levels. This meant we were in a proactive position to use the volatility seen in markets to our advantage.

Top equity contributors Computershare Ltd, Boral Ltd, and National Australia Bank. The largest detractors were News Corp, Iluka Resources Ltd, and Ampol Ltd. The Frame Futures Fund (FFF) declined by -0.88%. Equity & Fixed Income investments declined by -0.92% and -0.57%. Commodity and Currency investments rose by +0.47% and +0.35%.

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## Outlook

March will bring with it the first-rate hike for this tightening cycle. With inputs for key production commodities hitting recent highs, we do not expect inflation measures within the next few months to surprise the downside. Taking that into consideration, we are structuring our portfolios for an environment where we expect inflation to overshoot is prudent.


If you would like to discuss any of these points, please email me at [hue@framefunds.com.au](mailto:hue@framefunds.com.au) or call our office on 02 8668 4877.

All the best.

## HUE FRAME

Managing Director & Portfolio Manager

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# MARKET INSIGHTS

## FEBRUARY 2022

WRITTEN BY HARRY HEANEY

*In this issue of 'Market Insights', Harry covers how the global sanctions on Russia will impact the US Federal Reserve and what the implications are on inflation.*

Russia's recent invasion of Ukraine has sent global financial markets into a tailspin. Volatility in commodity, currency, fixed income, and equity markets has expanded, which has increased risk for all market participants. The remainder of this article will explore why markets are so concerned and what a 'worst-case' scenario may look like.

### What is happening?

Russia and Ukraine both play key roles in the global economy, particularly in the commodity space. Russia in particular supplies a significant proportion of the commodities required for global energy consumption.

They are the world's third-largest oil producer, the sixth-largest coal producer, and the second-largest gas producer. They provide ~40% of Europe's gas needs. Nornickel (MCX: GMKN), a Russian mining and materials production company, produces significant amounts of palladium, platinum, copper, and nickel.

When combined, Russia and Ukraine supply 29% of global wheat exports, as well as a significant percentage of corn and sunflower oil.



**HARRY HEANEY**  
Co-Portfolio Manager

In response to the invasion of Ukraine, many countries have placed sanctions on Russia. These sanctions will impact Russia's ability to do business on the international stage. Ukraine will also be impacted, as they focus on repelling the invasion. As a result, both nations will struggle to supply the world with these key commodities, and prices have begun to rise in response.

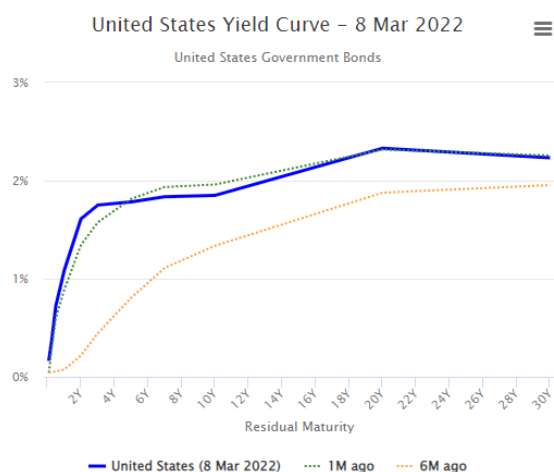
While some Russian supply will inevitably come to market via China, the final supply to the market should be lower than it was pre-conflict. Further sanctions, penalties, and trade embargos are expected to be placed in time and will continue to impact the supply of these commodities.

### Market Concerns

As input prices rise, producer prices increase, which results in further inflation. This will come at a time where many central banks have only just begun tightening after a period of historically loose monetary policy that has fuelled already elevated prices. Further pressure on prices could mean central banks may have to be more aggressive with their tightening schedule in order to meet their respective inflation mandates.

With global trade decreasing, prices rising, and the removal of liquidity through central bank operations, a slowdown in economic growth seems inevitable. This concern of stagflation is reflected in treasury markets, where the US yield curve has experienced significant flattening.

The 2s/10s spread currently\* sits at 23.5 basis points, compared to 61.75 basis points a month ago. This implies a market belief that the Federal Reserve will forge ahead with aggressive tightening over the next 12-24 months, which may stifle growth in the long term.



## Worst-case Scenario

In our opinion, prior to Russia invading Ukraine, the US Federal Reserve was treading on thin ice as they attempted to increase interest rates. They are in a challenging situation where they need to increase interest rates at a fast enough pace to contain inflation, however not increase too fast that it will impact growth and cause havoc to equity and housing markets. With the recent acceleration of key producer inputs, it seems inevitable that inflation is going to continue to accelerate over the next 12 months. Equity markets will need to adjust to an environment of higher interest rates as inflation runs above the long-run average.

All these issues point towards the increasing likelihood of a double-dip recession. As central banks tighten policy in the face of a deteriorating global economy, consumers will save more, and lines of credit for

businesses will dry up. This will result in a drain of liquidity from the financial system. In particular, equity and property markets may face serious headwinds, as higher interest rates offer more attractive investment opportunities for less risk.

In our opinion, it would take equity markets some time to recover from this scenario. Inflationary pressures would have to peak then subside, and the effects of the end of 'free money' would have to ripple throughout the financial system. This could mean lower property prices and equity valuations, particularly in businesses that use excessive leverage to fund growth.

We will be carefully monitoring the situation in Ukraine for the impact it is having on input prices and consumer inflationary expectations. Sustained trade issues between Russia and the West, as well as an uptick in consumer inflation concerns, could signal an increased likelihood that a double-dip recession is around the corner.

\*March 8, 2022.

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# GLOBAL MACRO

WRITTEN BY HUE FRAME

## Frame Futures Fund

Units of the Frame Futures Fund declined by -0.876%. The Fund's trading strategies generated +2.50%, while the core strategy declined by -3.16%.

Equity and Fixed Income investments declined by -0.92% and -0.57% respectively. Currency, and Commodity investments rose by +0.35% and +0.47% respectively.

February saw Russia invade Ukraine, which accentuated the volatility seen in January. In an environment which was already concerned with inflationary risk, the invasion of Ukraine, and the subsequently imposed sanctions on Russia caused some key commodities to rise swiftly. Oil, Wheat, Corn and Natural Gas rose by +8.70%, +21.94%, +11.43% and +13.33% respectively, as Russia is globally a large producer of these commodities. Gold and Silver rose by +6.22% and +8.88% respectively, as investors rushed to physical safe havens. The S&P 500, Nasdaq and Dow Jones Industrial Average all declined by over -3.00%. The S&P/ASX 200 outperformed relatively to its peers, it rose +1.11%.

Largest contributors to performance were our active trading on the S&P/ASX 200 Future contract, Corn Futures trading and an investment in an ASX junior gold explorer. They contributed +2.47%, +0.70% and +0.46% respectively. Largest detractors were our investments in the Moex market and ASX listed technology businesses.

In terms of fund activity, we initiated a position within the Chilean share market, traded out of our Natural Gas & Corn positions. We also took advantage of expanded volatility by trading the Russian Ruble, Nasdaq, and S&P 500 Future contracts.

Our focus now turns to the upcoming US Federal Reserve meeting and further inflationary data from the US. We remain defensive and look to use any market volatility to our advantage.

At the conclusion of the month, the Fund held 21 investments.

## INVESTMENT TEAM



**HUE FRAME**  
Portfolio Manager



**HARRY HEANEY**  
Research Analyst

## FUND PERFORMANCE as at 28<sup>th</sup> February 2022

	1 month	3 months	6 months	1 year
<b>Frame Futures Fund</b>	<b>-0.88%</b>	<b>-3.17%</b>	<b>1.79%</b>	<b>6.81%</b>
RBA Cash Rate + 3%	0.24%	0.78%	1.57%	3.14%
<b>Excess Return</b>	<b>-1.11%</b>	<b>-3.96%</b>	<b>0.22%</b>	<b>3.67%</b>

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# AUSTRALIAN EQUITIES

WRITTEN BY HARRY HEANEY

## Frame Long Short Australian Equity Fund

Units of the Frame Long Short Australian Equity Fund increased +3.16% in February. Comparatively, the S&P/ASX200 rose by +1.11% over the same period.

February was a very busy month in terms of half-year company reporting and news headlines. The month began with hawkish pivots from global central banks about inflation concerns. The Reserve Bank of Australia held their first meeting of the year, where they noted inflation and the labour market were both running hotter than expected. As a result, they chose to end their asset purchase program, stemming the flow of additional liquidity to the bond market.

Towards the middle of the month, tensions between Russia and Ukraine reached boiling point when President Putin declared separatist regions of Ukraine independent and sent in 'peacekeeping' forces. This culminated in a full-scale Russian invasion of Ukraine that has been met by harsh financial sanctions from western nations. After an aggressive initial sell-off, the market is still attempting to accurately price the impact of these sanctions and the possibility of further escalation.

Fortunately, our aggressive risk management practices in January paid dividends last month. Our reduced exposure meant we were sheltered from some of the considerable volatility that plagued the market. The strategy continued to exit positions as tight risk measures remained in place. We feel comfortable continuing to exit the market and being underinvested in the current geopolitical environment. Over the course of the month, we increased our allocation to the discretionary active trading strategy. This strategy contributed +2.07% to the final performance.

Top contributors were Computershare Ltd (ASX: CPU), Boral Ltd (ASX: BLD) and National Australia Bank Ltd (ASX: NAB), which contributed approximately +0.61%, +0.39% and +0.33% respectively. Computershare upgraded full-year earnings guidance after strong revenue growth and cost controls fuelled margin expansion. Boral returned \$3 billion to shareholders via a cash distribution and dividend after the sale of several building product businesses. NAB benefitted from reweighting into the financial sector.

The largest equity detractors were News Corp (ASX: NWS), Iluka Resources (ASX: ILU), and Ampol Ltd (ASX: ALD). They detracted approximately -0.15%, -0.12% and 0.06% respectively. All three companies were disappointed with their half-year reporting results. We have since exited these positions.

At the conclusion of the month, the fund held 5 equity investments.

## INVESTMENT TEAM



**HARRY HEANEY**  
Co-Portfolio Manager



**HUE FRAME**  
Co-Portfolio Manager

### FUND PERFORMANCE as at 28<sup>th</sup> February 2022

	1 month	3 months	6 months	1 year
<b>Frame Long Short Australian Equity Fund</b>	<b>3.16%</b>	<b>-1.61%</b>	<b>-7.45%</b>	<b>-2.72%</b>
RBA Cash Rate + 3%	0.24%	0.77%	1.55%	3.14%
<b>Excess Return</b>	<b>2.92%</b>	<b>-2.37%</b>	<b>-8.99%</b>	<b>-5.86%</b>

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# COMPANIES IN FOCUS

WRITTEN BY SYDNEY ROBERTSON

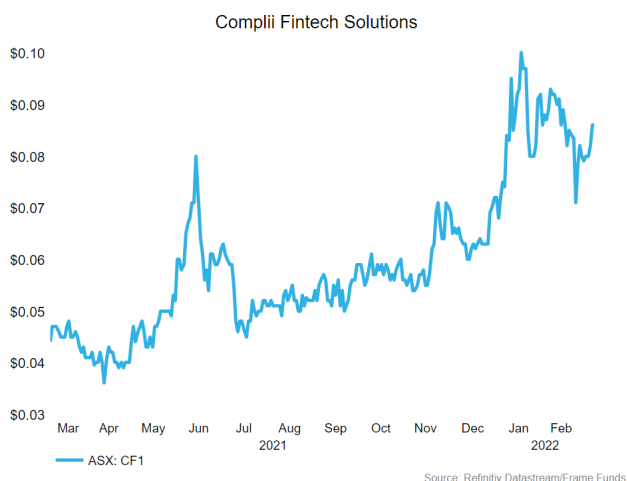
The 'ASX Companies in Focus' section provides an update on a selection of companies that may be held within the Frame Futures Fund and the Frame Long Short Australian Equity Fund.



**SYDNEY ROBERTSON**  
Research Analyst

## Complii FinTech Solutions (ASX: CF1)

Complii FinTech Solutions (ASX: CF1) is a compliance centric technology company focusing on the transition from paper-based compliance systems. Their core product automates the sending of a Statement of Advice (SOA) and Records of Advice (ROA), 708 investor certificate expiry, Future of Financial Advice (FOFA) letter auto-generation, along with managing operational walls and internal compliance. Their product offering also extends to its client relationship management system and their recently released 'Corporate Highway', which provides a platform to place deals for integrated brokers and Australian Financial Services Licensees (AFSL), along with underlying users to bid on.



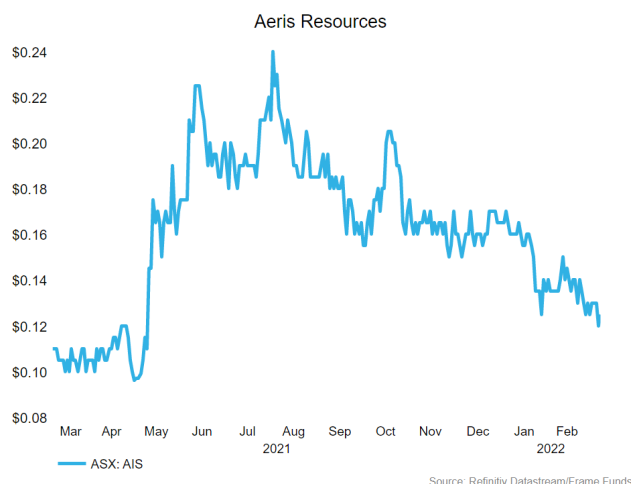
Fundamentally the company's development orientated focus, recent acquisition, and market share has provided it with the ability to increase their on-going revenue and recently, become cashflow positive. The recent acquisition of Primary Markets was a significant driver in transactional and ARR revenue growth. Even though CF1 only accounted for the Primary acquisition for about a third of its' reporting period, Primary contributed significantly to their reported revenue.

Complii's near term growth hinges on the growth of their

recent acquisition, Primary Markets. The continued rolling out of its core product across AFSL holders will also allow for cross selling of its current product offering. We also look keenly monitor the company's proposed expansion into Asia – namely Singapore and Hong Kong. We look forward to the upcoming FY22 report to see if the integration of Primary has run ahead of expectations.

## Aeris Resources (ASX: AIS)

Aeris Resources (ASX: AIS) is a mid-tier diversified miner, with two wholly owned assets – the Tritton Copper Mines, and the Cracow Gold Operations. Further to this, Aeris has two joint-ventures, the Canbelego JV (30% stake) with Helix Resources (ASX: HLX), predominately testing for copper and the Torrens JV (70% stake), which is exploring for iron-oxide copper-gold (ICOG).



Due to the current macroeconomic theme of increased demand for base metals, AIS has focussed their attention on their copper assets. Globally, there is restricted supply of copper due to a lack of new, high-grade deposits.

These factors, in combination with the transition to renewable energy (copper is a key component to



battery production) ensure that copper should remain well bid moving forward.

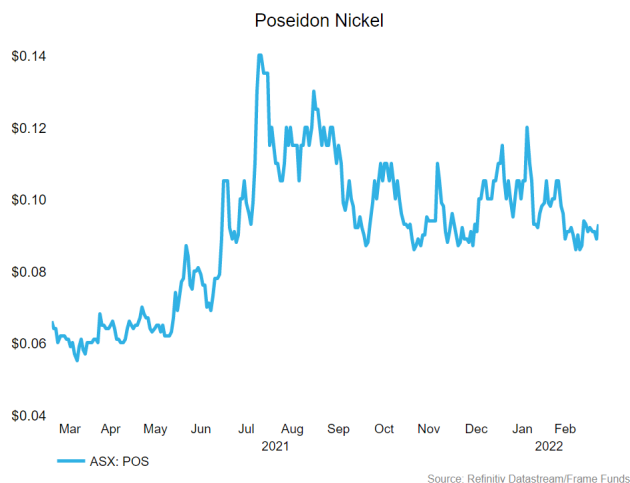
The 100% owned Tritton Copper deposit looks to produce between 18.5-19.5kt at an AISC between \$4.60-\$4.85/lb. Cracow is targeting to produce between 64-66koz at an AISC between \$1,650-\$1,700/oz. In our view, their guided AISC and production numbers should be hit (pending disaster), so any additional resource expansion, commodity price rise or deposit acquisition, should be viewed positively by the market.

### Poseidon Nickel (ASX: POS)

Poseidon Nickel Limited (ASX: POS) is a nickel sulphide development and exploration company with three operational projects near Kalgoorlie. Specifically, Poseidon owns the Black Swan, Mt Windarra and Lake Johnston Nickel Sulphide projects, two of which contain processing plants. Future projects include the construction of a gold reprocessing facility, although with an increased focus on Nickel, the company is seeking a joint venture partner. Although Poseidon is considered a pure-play nickel miner and producer, in its' Mt Windarra site contains a ~180koz gold resource.

The macroeconomic rationale for Poseidon is similar to Aeris Resources (AIS). Nickel is a key component of battery production, while also being a key input for stainless steel production (used in infrastructure). The Nickel price has climbed significantly over the last 12 months, which makes the feasibility studies of the Black Swan project better, which in turn improves the outlook for the business of Poseidon. Recently, with the invasion of Ukraine, the Nickel price has soared.

This is due to Russia and Ukraine being key global producers of the metal. With sanctions being placed on Russia, further disruptions to the global supply of Nickel is anticipated. Although painful in the short term, a move away from Russian reliance on these metals is anticipated and should benefit Poseidon.



Looking forward, we await the results of increased production at the Black Swan project, and the conversion of Golden & Silver Swan resources into JORC defined resources. Further drilling results where high grades of Nickel are found may also provide a catalyst to further price rises.

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Frame Funds.

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