
Keeping you up to date with financial markets
and Frame Funds.



June 2022 // Issue 16

IN THE FRAME

RENEWABLE ENERGY'S PROBLEM

FUND PERFORMANCE

How our strategies performed in May

GLOBAL CENTRAL BANKS IN A PICKLE

What needs to be done to get inflation under control

WHAT I SAW MAY 2022

WRITTEN BY HUE FRAME

In this issue of 'What I saw', Hue covers the on-going energy shortage, the recent RBA rate rise, and how our strategies performed in May.

The RBA increased interest rates by 25 basis points as Governor Lowe emphasised that there was a need to return to a normal monetary policy environment. In the United States, Jerome Powell of the Federal Reserve increased interest rates by 50 basis points and mentioned that further rate rises were on their way.

At time of writing, interest rates in the US are at 1.75%, with interest rate markets pricing in a further 1.25% increase by the end of September.

Energy shortage

Coal prices continued to climb aggressively over the course of the month, as energy shortages hit home across the globe. The Russian Ukraine war has accelerated these shortages, as numerous nations have implemented sanctions on the oil & gas supply from Russia. Harry Heaney covers this in more detail within the Market Insights section.

Portfolio performance

During May, both strategies suffered as markets broke to new lows and volatility continued to expand within global equity markets. The Long Short Australian Equity declined by -8.64%, while our global macro strategy declined by -7.25%.

Both strategies have experienced periods of expanded volatility as markets have whipsawed, however both strategies are still comfortably within their tested peak to trough decline analysis.

Top equity contributors for the Frame Long Short Australian Equity Fund (FLSAEF) were Whitehaven Coal Ltd (**ASX: WHC**), Worley Ltd (**ASX: WOR**) and Atlas Arteria Group (**ASX: ALX**). They contributed +0.30%, +0.16% and +0.12% respectively.

Largest detractors were Metcash Ltd (**ASX: MTS**), JB Hi-Fi Ltd (**ASX: JBH**) and Nufarm Ltd (**ASX: NUF**).



HUE FRAME
Managing Director & Portfolio Manager

The Frame Futures Fund (FFF) declined by -7.27%. Equity, Commodity and Fixed Income investments declined by -6.26%, -0.64% and -0.58% respectively. Currency investments added +0.70%.

Readers will notice that the strategy has had reasonable contributions from all asset classes beside equities as of late, however with equity market conditions reaching extreme levels (in the short term), we expect a reversion to the mean to occur shortly.

Outlook

With the US Federal Reserve now adjusting their expectations for further interest rate increases in line with current market pricing, we anticipate that a short-term bottom (in equity markets) may be near. However, like we saw in the 1970's, aggressive interest rate increases do not reduce inflation immediately and can take some time to work its way through the economy and reduce the demand side of the equation.

MARKET INSIGHTS

MAY 2022

WRITTEN BY HARRY HEANEY

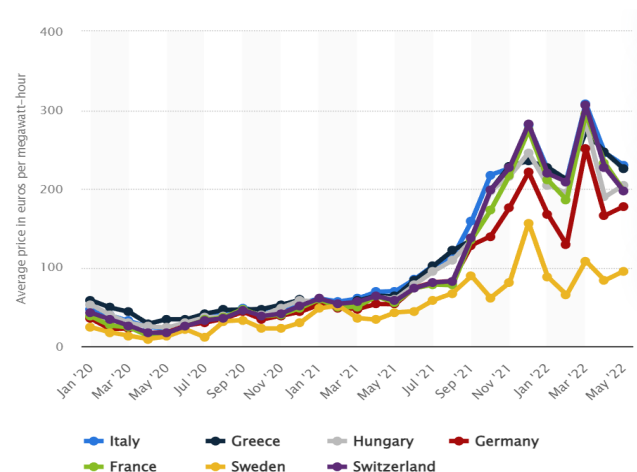
In this issue of 'Market Insights', Harry covers the on-going energy shortage, the impacts on Europe, the United States and Australia. He also covers what is the possible net result of the current situation.

At the start of the year, we published our annual [Investment Themes Worth Backing](#) document, which identified underinvestment in coals and gas as a 'tactical' theme to watch. The theme was based on mass global investment in the transition to renewable energy leaving fewer dollars to be spent on existing fossil fuel power sources. The war in Ukraine and resulting sanctions on Russian energy commodities has since tightened an already strained global energy market to the point of breaking.

The remainder of this piece will discuss how the theme has played out around the world.

Europe

European nations have undoubtedly been the hardest hit by the lack of oil and gas supply from Russia. Energy markets in the Eurozone were already stretched thin off the back of heightened post pandemic demand, a drop in renewable power generation due to low wind speeds, and high coal and gas prices. Most European countries experienced record electricity prices in December 2021, with prices per megawatt-hour spiking to more than three times December 2020 levels.



HARRY HEANEY
Co-Portfolio Manager

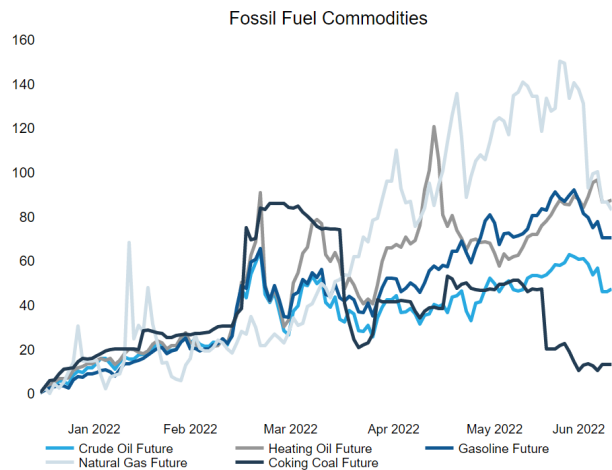
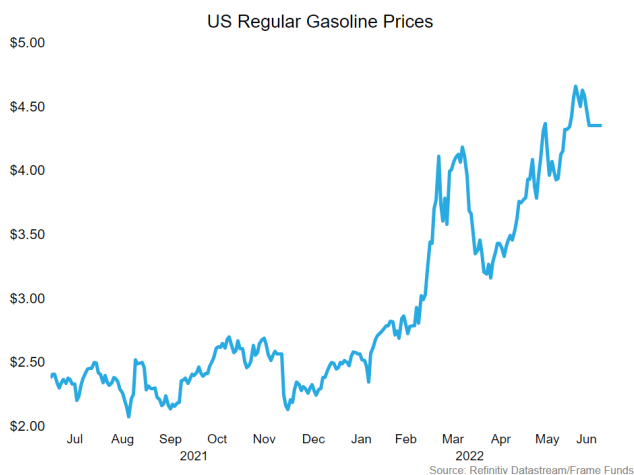
Prior to their invasion of Ukraine, Russia supplied approximately a quarter of the oil EU countries imported and 40% of all natural gas imports. Germany, Europe's largest economy and the 4th largest economy in the world, relies on Russia for almost half its gas supply. This was to be a short term 'fill in' as they transitioned to renewable energy sources – Germany has pledged to have 65% of its power coming from sustainable energy sources by 2030.

With the EU planning to reduce Russian gas imports by two thirds by the end of the year, and Moscow cutting capacity on the main gas export pipeline to Berlin by 60%, Germany is in a bind. So much so, they have recently announced they are increasing coal use to reduce reliance on gas for electricity generation. It is not just Germany however - Italy is reportedly on the verge of declaring an emergency gas alert if supplies are not restored by Russia.

United States

The United States (as the world's largest oil and gas producer) has been somewhat sheltered from the impacts of the Russia-Ukraine war. That being said, higher oil and gas prices have placed strong upward pressure on inflation and have hit the American consumer in the hip pocket.

President Biden has dipped into the nation's Strategic Petroleum Reserve three times since the invasion to calm raging prices. He has also published an open letter to oil producers and refiners, pleading with them to increase production and alleviate pressure on consumers.



For their part, the United States oil lobby, headed by the American Petroleum Institute has made their own demands of the White House. They include easing restrictions on federal oil and gas lease sales, the speed up of permit approvals and a reduction of required climate disclosures for projects. The underlying theme from producers and refineries seems to be a reluctance to make investments in long term assets without a firm commitment from the top levels of U.S. government that they will still be needed after this crisis passes. This is as opposed to being punished with higher taxes and regulations the moment the desperate need for oil and gas passes.

Australia

The energy grid on the east coast of Australia has also come under intense pressure in recent weeks. The combination of a shortage of coal and routine maintenance closures caused prices in the spot market to spike above capped levels, causing the Australian Energy Market Operator to suspend trading. Soaring market prices for coal and gas mean those producers that are having to purchase in the open market are downgrading guidance. Origin Energy (**ASX: ORG**) is a prime example – their Energy Markets Underlying EBITDA is now expected to come in around \$310 - \$460 million, compared to the previously guided \$450 - \$600 million. Australian coal fired power station operators are also bringing forward closure dates for their plants as they forecast less demand for fossil fuel use in the future.

What is the net result?

Predictably, the net result has been higher fossil fuel prices. Crude oil, heating oil, gasoline, natural gas and coal prices have all spiked dramatically so far in 2022, further exacerbating global energy woes.

However, one thing that has been made abundantly clear is the need for a proper transition plan to renewable energy. In our view, this transition needs to be planned on a global scale, rather than every country for itself.

Is the global transition to renewable energy inevitable? Definitely.

Will fossil fuels play a key role in power generation until such a time? Unfortunately so.

GLOBAL MACRO

WRITTEN BY HUE FRAME

Frame Futures Fund

Units of the Frame Futures Fund declined by -7.25%. The Fund's trading strategies declined by -2.95%, while the core trend following strategy declined by -4.30%.

Equity, Commodity and Fixed Income investments declined by -6.26%, -0.64% and -0.58% respectively. Currency investments added +0.70%.

Largest contributors to performance were investments in the iShares MSCI Chilean ETF, Mexican Peso USD Future contract, and a short position on the Lumber Future contract. Largest detractors were equity investments in the Australian share market and a long position on the Micro-Bitcoin Future contract amongst others.

In terms of fund activity, we continued to reduce exposure out of global equity markets. Volatility has risen, which has expanded our carried equity risk.

Looking forward, we continue to monitor how inflation responds to further interest rate increases. We will be looking for a leveling of headline inflation to occur before actively looking at additional positions in our long portfolio.

At the conclusion of the month, the Fund held 24 investments.

INVESTMENT TEAM



HUE FRAME
Portfolio Manager



SYDNEY ROBERTSON
Quantitative Research Analyst

FUND PERFORMANCE as at 31st May 2022

	1-Mth	6-Mth	1-Yr	2-Yr p.a	3-Yr p.a
Frame Futures Fund	-7.25%	-14.30%	-10.72%	9.50%	5.18%
RBA Cash Rate + 3%	0.28%	1.55%	3.14%	3.19%	3.26%
Excess Return	-7.53%	-15.85%	-13.87%	6.31%	1.92%

Past performance is not an indicator for future performance. This is not intended to be financial advice and does not take into account any particular person's circumstances. Before relying on this information, please speak to an independent financial adviser.

AUSTRALIAN EQUITIES

WRITTEN BY HARRY HEANEY

Frame Long Short Australian Equity Fund

Units of the Frame Long Short Australian Equity Fund decreased -8.64% in May. Comparatively, the S&P/ASX200 declined by -3.01% for the month.

The Australian share market continued to struggle in May. The month began with the RBA increasing interest rates 25 basis points. Governor Lowe highlighted the need to return to a 'business as usual' monetary policy environment, given inflation and growth were running ahead of the Bank's forecasts. Equity markets fell as investors digested the beginning of quantitative tightening and further interest rate hikes. Realised volatility remained high over the month with no sectors exhibiting strong outperformance.

Top equity contributors for the month were Whitehaven Coal Ltd (**ASX: WHC**), Worley Ltd (**ASX: WOR**) and Atlas Arteria Group (**ASX: ALX**). They contributed +0.30%, +0.16% and +0.12% respectively. Coal prices continued their charge higher as energy shortages persisted around the globe. Worley announced several new contracts over the course of the month which benefitted their share price. Atlas Arteria moved higher off the back of increased travel as the world continues to move past the COVID-19 pandemic.

Largest detractors for the month were Metcash Ltd (**ASX: MTS**), JB Hi-Fi Ltd (**ASX: JBH**) and Nufarm Ltd (**ASX: NUF**). They detracted approximately -0.42%, -0.42% and -0.39%. All three businesses suffered at the hands of a gloomy global outlook spurred on by unsustainably high prices and poor sales prospects. We have since exited our investments in Nufarm and Metcash.

As volatility remained high and the global growth outlook worsened, we began to reduce equity exposure. We exited several of our positions in the materials space while retaining our energy exposure as global supply remains tight.

At the conclusion of the month, the Fund now held approximately 39.69% in cash and had 27 investments.

INVESTMENT TEAM



HARRY HEANEY
Co-Portfolio Manager



HUE FRAME
Co-Portfolio Manager

FUND PERFORMANCE as at 31st May 2022

	1-Mth	6-Mth	1-Yr	2-Yr p.a	3-Yr p.a
Frame Long Short Australian Equity Fund	-8.64%	-9.03%	-14.87%	-	-
RBA Cash Rate + 3%	0.28%	1.58%	3.17%	-	-
Excess Return	-8.92%	-10.61%	-18.04%	-	-

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