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Q2 2022 Update

Fund and Market Recap

Second quarter 2022 completed a very difficult first half of the year for financial markets of almost all asset classes. Equity markets had their worst start in more than 50 years. Fixed Income markets lost double digit percent in value. Crypto currency lost over 50% of their value. All of this was driven by the federal reserve raising interest rates to cool inflation from its highest levels since the 1980's.

While commodity markets held up much better than most market segments, there was a dramatic selloff towards the end of the quarter as concerns over a recession heightened dramatically.

Our primary investment in the fund continues to be in the energy industry. This investment sold off in tandem with the oil markets. Additionally, it's merger closed on July 1 that resulted in certain owners rebalancing their positions, selling into a very bad market. The result of this was the company trading to extremely attractive valuation levels. We used this selloff to invest some of our excess cash as we see dramatic upside over the next 12 months.

Economic Performance and Outlook

Inflation has become the first, second and third concern for the federal reserve. Market speculation is rampant as to how high the fed will have to raise interest rates to cool the economy and get inflation back to target levels. Economic performance is beginning to show signs that fed policy is having its desired impact. Higher interest rates are slowing down a wide variety of sectors through tighter and more expensive credit. However, the employment dimension of the economy continues to be very healthy, showing up in the job growth numbers.

Recent corporate surveys have shown that the number one concern of corporate management continues to be staffing. These same surveys found that while hiring might slow, the economy would need to get dramatically worse before layoffs would increase to any meaningful degree. So, while it is a difficult exercise, there is reason to be optimistic that the fed will be able to get inflation under control without causing a recession. Furthermore, if there is a recession, we do not expect it to be anything like the '08/'09 recession. Personal and corporate balance sheets are in much better shape, the health of the financial system is as good as it's been over the last 50 years and the employment market is at a much different place.

Q2 2022 Return Information

Q2 2022			Full Year 2022		
LPG Cap Part (1)	HF Comp Ind (2)	Russell 2000	LPG Cap Part (1)	HF Comp Ind (2)	Russell 2000
-20.87%	-7.97%	-17.49%	-11.90%	-11.96%	-23.93%

(1) Certain expenses are estimated for quarterly returns; annual returns are actual
(2) Hedge Fund Composite Index the hedge fund index ticker HFREIHI as reported by Bloomberg

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Market Expectations

Given current valuation levels, we are as positive on the projected returns as we have been in the last 10 years. There are a multitude of extremely interesting opportunities to choose from. However, we also expect the markets to be volatile until there is more clarity on the economic outlook. We expect the Fed to do another 75 basis point interest rate hike and then wait to see the impact rate increases have on inflation and the economy. Given the Fed has interest rates much closer to where it wants them, there should be less market volatility around this issue going forward. If the economy can avoid a deep recession, it is our view that the bulk of the downside in equities has passed.

Fund Positioning

With the most recent selloff in the markets, we have had no trouble finding extremely interesting opportunities to invest in. We have been using our cash balances to average into positions and expect to continue to do so at current prices.

Investment Updates

Energy

Our investment in this space continues to exceed all business targets. At Oil prices substantially below current levels, our investment is set to produce record amounts of cash flow. Over the next 18 months, it will generate more than 50% of its equity market cap in FCF. Over half of this is expected to be used to buy back stock, which will be extremely accretive to our position.

Despite this, the stock did not perform well in the 2nd quarter. Forced selling around the close of the merger and a particularly weak market led to some attractive trading levels. We used this to add to our position. It is one of the more attractive opportunities we have seen over the last several years and expect it to perform well over the next 12 months.

Telecom/Media/Communications

At quarter end there have not been any major changes to our investment in this sector. Operations have progressed as expected, but it will be a while before this is reflected in the performance of our investment. We will continue to monitor trading levels to increase our position when it warrants.

Airlines

Trading levels for the equities in this space have come off dramatically, and we have dusted off our work. We are evaluating these opportunities against other potential investments and will be judicious with our entry. Again, primary concern is how they handle the debt incurred over the last 2 years to survive the covid lockdowns.

Outlook

While market volatility increased again during the 2nd quarter, we view the environment that caused this to be abating. Valuations are at very attractive levels. A much more measured increase in interest rates after July should lower volatility going forward. Given our expectations for strong operating performance from our investments, we are looking for good returns for the balance of the year.