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LPG INVESTMENT MANAGEMENT

Q2 2023 Update

Fund and Market Recap

Second quarter of 2023 saw several of the risks that drove volatility and negative performance in the first quarter play out without major negative impact to financial markets. Regional banking issues that had reminded investors of the financial crises of ‘08/’09 were resolved without having a major impact on the economy. Inflation cooled down from the beginning of the year, providing hope to the markets that the Fed is getting close to the end of the current hiking cycle. Employment numbers continue to be solid, but not so strong that they will drive inflation. Markets overall are beginning to embrace the idea that we might experience a soft landing.

Our fund benefitted from the recovery in the markets. Our energy position continues to do quite well operationally and financially. We also took advantage of the volatility to build a healthy position in the Telecom/Media space and had a quick trade work out in the regional banking space.

Economic Performance and Outlook

Knock on wood, but the Fed looks to be threading the needle with the economy. Three months ago, the markets were extremely pessimistic about the soft-landing market thesis. All the economic numbers during the quarter point to this outcome being the most likely scenario. Inflation is heading quickly to the Fed’s target; employment continues to be resilient and regional banking issues look to be mostly contained.

Market Expectations

What a difference three months make. With a healthy bounce from the lows hit during the first quarter, our expectation of solid single digit positive returns look conservative. At this point, double digit returns for the broad equity markets look very achievable. Fixed income markets should stabilize as the U.S. looks to have already passed peak interest rates across the treasury yield curve. With this, volatility should stay low, helping markets continue their upward trajectory in the second half of the year. This is all predicated on the soft-landing economic theme working out.

Fund Positioning

With the strong rally in the markets, we have taken steps to monetize our energy investment and deploy the cash in other opportunities. We took advantage of the sell-off in regional bank stocks, built a healthy position in a media company and have a nice cash position. Thanks to current short-term rates, our cash will generate a reasonable return until our shopping list reaches attractive valuation levels.

Q2 2023 Return Information

Q2 2023			Full Year 2023		
LPG Cap Part (1)	HF Comp Ind (2)	Russell 2000	LPG Cap Part (1)	HF Comp Ind (2)	Russell 2000
19.26%	2.87%	4.78%	10.59%	5.45%	7.24%

(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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Investment Updates

Energy

During the quarter, our investment announced an acquisition that helps position it to improve operationally and accelerate cash flow growth. It continues to generate large amounts of excess cash flow and uses it to the benefit of stockholders. While it is still an attractive opportunity from a valuation standpoint, we have begun to monetize our investment as it reaches our valuation targets. Macroeconomic performance looks to continue to support the industry and our investment.

Telecom/Media/Communications

During the quarter, we built a healthy position in the bonds of a cable company that we expect to generate over 30% annualized returns over the next several years. As previously discussed, the company is rebuilding its distribution network in order to be able to provide fiber services to most of its customers. This has resulted in the company going from generating very significant excess cash flow to almost zero. As it completes this rebuild over the next 24 months, we look for it to return to generating substantial cash flow and pay down debt, driving the performance of our investment.

Outdoor Recreation

This sector continues to rank high on our shopping list. However, we view the catalysts that will drive performance to be too far out at this point to justify an investment.

Regional Banks

After substantial work on the sector, we made a few investments that we found to be particularly attractive. However, we did not last long as equity prices recovered, and valuations no longer justified exposure given the substantial operational risks that remain in the sector.

Leveraged Equities

Over the next 12-24 months, we expect this space to get particularly interesting. There are several industries that look vulnerable to debt that was incurred during the low interest rate environment that is no longer. Maturity walls look like they are a few years out, but when we get there, things should become significantly more attractive.

Outlook

As we move through the second half of the year, a soft economic landing looks very plausible. If the Fed can manage this, more upside to the markets looks very likely. We will be watching to make sure that this actually happens and respond accordingly.