Midstream: fears about recession, the Fed, and oil demand have sucked the oxygen out of almost every investment discussion. While the consensus narrative holds that these factors will determined the outcome of energy investments, historical data suggest this focus is misplaced. Fed policy, recessions, and demand destruction have historically coincided with lower inflation and falling oil prices… 50% of the time. So these variables have historically been no better indicators than a coin-flip. Next week, we will publish a white paper on 60+ years of economic history, and a study on which variable does matter. Email us to receive a copy.

Natural Resources: Elevated oil prices have heightened investor focus on recessionary risks and increased global inflationary pressures. Investors looking for similarities to historical time periods often cite peak oil prices of 2008. However, given the current strength of the US Dollar, many global economies have already been facing higher-than-2008-peak oil prices, with limited demand impact to date. Additionally, non-US oil demand has benefited from high global natural gas prices resulting from the Russia/Ukraine conflict.

Access Recurrent's new White Paper on the rising "risk premium" in the oil market
Access Recurrent's latest video on the impact of Russia's invasion

MLP & Infrastructure

Performance review

During the month of June 2022, the Recurrent MLP & Infrastructure Strategy generated net returns of -14.02%, roughly in-line with the Alerian MLP Index's (AMZ) -13.95% return. Since the strategy's July 2017 inception, Recurrent's MLP & Infrastructure Strategy has outperformed the AMZ by +6.04% (annualized, net of fees). Please see the performance section at bottom for more detail.

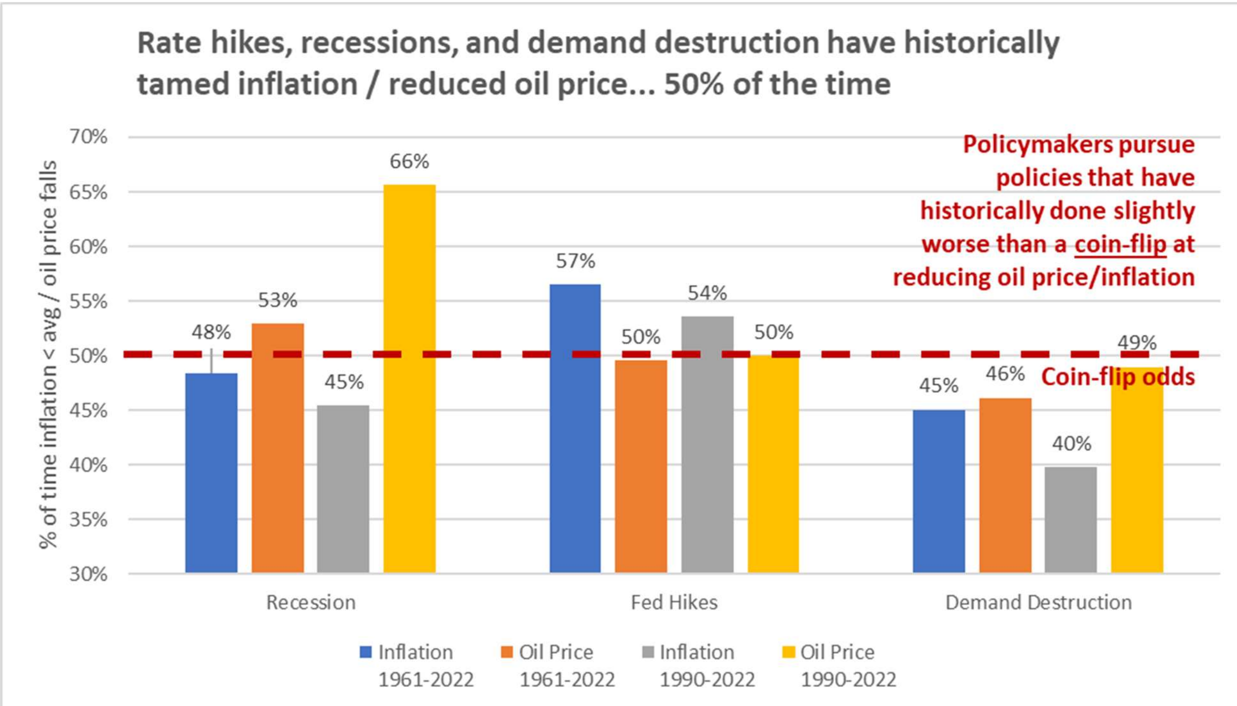
Concerns around a potential recession, Fed hikes, and demand destruction dominate every conversation…

Slowing global economic growth and concerns about the Fed potentially overreacting to inflation after admitting its "policy mistake" in allowing inflation to rise post-COVID have sucked all of the oxygen out of energy investor discussions. Last week's Energy Information Administration (EIA) release has led to questions about whether we are entering a period of slowing oil demand, given sustained high pump prices.

…but should these concerns be our sole focus as energy investors?

We believe that the data suggest these 3 concerns may matter less for oil markets, and in turn for energy investors, than consensus wisdom holds. While the "consensus" narrative holds that Fed hikes, Recessions, and "Demand Destruction"/conservation are unmitigated disasters for the oil industry and energy investors, reality is not as straightforward as the narrative.

As we see below, recessions have pushed inflation rates to below-median levels roughly 48% of the time since 1961. Fed hikes are slightly more effective, with hikes coinciding with below-median inflation 57% of the time since 1961 (although slightly less effective at 54% since 1990). Finally, demand destruction is the least effective long-term tool against oil prices and inflation (inflation only falling 45% of the time), as demand destruction occurs during sharp increases in prices, and demand returns as consumers become more accustomed to higher price levels.



Source: Recurrent research, Bloomberg data

So what actually matters for the inflationary cycle?

We are glad you asked! Next week, we are releasing a new Recurrent White Paper covering 60+ years of history, with an examination of the interplay between the Fed, the energy industry, and the inflationary cycle. We believe that only **one key variable** matters for inflation, and in turn for the profitability of the energy sector (and its appeal as an investment). Hint: the variable is not GDP growth, Fed policy, or demand destruction. Shoot us an email to receive a copy.

Natural Resources

Performance Review

In the month of June 2022, the Alma Recurrent Global Natural Resources Fund fell -16.94% (net), more than the S&P Global Natural Resources Index's -15.77% gross decline. Economic recession fears caused economically sensitive sectors to fall more than the benchmark. Aluminum, copper, chemicals and steel sectors all fell more than 25% in the month, and all are overweight relative to the benchmark. Energy, agriculture and paper sectors fell less than the benchmark, and added value relative to the benchmark during the month.

Investment Discussion

In the last several months, the combination of economic uncertainty and rapidly increasing interest rates have caused the US Dollar to strengthen relative to global currencies, particularly since the middle of 2021.

US Dollar vs Global Currency Basket, 15-year chart

Source: Bloomberg, Recurrent Research

Since COVID, energy commodities have appreciated, due to strong demand recovery, combined with undersupply due to underinvestment. In March 2022, Brent oil prices peaked above $130/barrel, as the early stages of the Russia/Ukraine conflict combined with increased seasonal demand. More recently, oil prices have reverted closer to $100/barrel, reflecting weakening economic growth due to high inflation.

Brent Crude Price, 15-year chart

Source: Bloomberg, Recurrent Research

From a global perspective, weakening oil prices are viewed as a clear positive from broader economic prospects. However, since oil transactions generally occur in dollars, the strengthening dollar has further increased the cost in many global economies. In fact, even though the price in dollar terms has fallen nearly 30% from March highs, since the dollar has strengthened by 7% during the same period, many global economies have not benefited to the same degree as the United States.

Furthermore, if we consider the longer-term impact of the strong dollar relative to other global currencies, recent oil price strength is even more noteworthy. In US Dollar terms, the Brent crude oil peak price of $145.66 was on July 3rd, 2008. However, since July 2008, the relative strength of the USD has caused the price to rise by 147% in Brazilian Real terms!

Brent Crude Price in Brazilian Reais, 15-year chart

Source: Bloomberg, Recurrent Research

The same dynamic is present in many global currencies and economies, as seen in the table below:

	Current Brent Crude Price in Local Currency	Previous 2008 Peak Price	% Change since 2008
Australia	156	152	3%
Brazil	577	234	147%
Canada	149	137	9%
Denmark	780	700	11%
Euro	105	93	13%
Great Britain	88	74	20%
Indonesia	1,574	1,322	19%
India	8,348	6,300	33%
Mexico	2,165	1,510	43%

Source: Bloomberg, Recurrent Research

While many investors appropriately note that the high prices of 2008 led to demand falling slightly as the global economy shrunk during 2009 during the financial crisis, it is important to also note that demand had fully recovered within 18 months. Although not reaching peak levels again, Brent oil prices remained strong for several years.

While Russian oil production has remained available to global markets, the removal of Russian natural gas has had a significant impact on oil markets

We believe one underestimated oil demand driver is high global natural gas prices, which is the result of the Russia/Ukraine conflict. Without Russian natural gas supplying Western Europe, European and Asian users of natural gas are competing for scarce waterborne LNG shipments, increasing prices. As of July 13, 2022, the benchmark price of natural gas in Europe and Asia is $50/mmbtu and $39/mmbtu, respectively.

Oil remains attractive when comparing the price of oil vs natural gas on a BTU equivalent basis

From an oil perspective, in many parts of the world, industrial and utility consumers look to use the least expensive fossil fuel per BTU to power their business. The quick rule of thumb to equivocate the BTU cost between oil and natural gas is to multiply the natural gas price by 6 to approximate the BTU content of a barrel of oil. Therefore, in Europe and Asia, the natural gas equivalent of a barrel of oil costs $50/mmbtu x 6 =$300 and $39/mmbtu x 6 = $234/barrel, respectively, much higher than the cost of a barrel of oil. As a result, for companies with the ability to choose the cheaper fuel would choose oil over natural gas, boosting global demand for oil.

Given recent elevated oil prices, many investors have looked to the post 2008 peak oil price period as an analogue, when demand fell causing prices to fall during the financial crisis. While similar in that today's elevated price of oil has heightened growth concerns, we believe there are two main differences. Firstly, global economies have long experienced oil prices higher than 2008 peaks due to the strength of the US Dollar, with little demand impact. Secondly, during the 2008 financial crisis, global natural gas prices generally moved in sync with oil prices, so there was little change in oil demand due to fuel switching. Today, reduced natural gas supplies due to the Russia/Ukraine conflict has increased natural gas prices, and driven industrial users to oil as a cheaper equivalent on a BTU basis.

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