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Blackfinch Group

Russia-Ukraine Conflict

February 2022

While Russian tension with Ukraine has been simmering for years, this week's military action from President Putin has escalated hostilities to levels that threaten peace within Europe and has already tragically resulted in the loss of life.

As investment professionals, it's our responsibility to assess the potential impact on financial markets and the global economy. While we monitor the developments, the only thing that can be said with certainty is that no one knows what Putin will do, or the effect it will or won't have on the market.

In global market terms, we know from history that while geopolitical crises such as this one can roil markets, they usually don't have longer-term consequences for investors. However, we do not underestimate the risks presented by Russia's role as a global energy provider. Russia is the source of 10% of the world's energy, and nearly 50% of the energy consumed in Europe, therefore the risks extend far beyond the borders of Russia and Ukraine, including higher energy prices and increased financial market volatility. Indeed, it's fair to say that investment markets have already priced in significant levels of risk and consequence due to this factor.

I've asked my investment teams across the Blackfinch Group to share their insights into current events, and how they relate to their portfolios, starting with Blackfinch Asset Management.

Blackfinch Asset Management

Although we do not have a direct asset allocation to commodities, our recent portfolio shifts in favour of more value-based sectors, along with our reintroduction of the FTSE 100 last year, should help us to capture some of the upside we are currently seeing in energy markets. Yields are higher in these markets, which will also help our portfolios. While the FTSE 100 index is down, it is still outperforming broader European benchmark equity indices, at the time of writing, due to its higher energy sector exposure. There are still supply-side constraints within energy markets that do not look to be easing any time soon so if we do consider any short-term tactical positions, it most likely would be towards value stocks, energy markets and high yielding sectors.

Blackfinch Adapt AIM Portfolios

We continue to follow our normal process of daily monitoring of price movements and news flow across the Blackfinch Adapt AIM Portfolios. Further volatility can be expected in UK markets in the short term, due to the uncertainties regarding the impact of the Russian invasion. Stocks listed on the Alternative Investment Market (AIM) are typically closely correlated with overall short term market movements, and we have already seen some depreciation in portfolio values because of recent events, albeit to a lesser extent than the overall market.

At Blackfinch, most companies in our AIM portfolios are based in the UK and we have no direct exposure to Russia or to the armaments industry. We use RepRisk to continuously monitor any environmental, social and governance (ESG) events related to any of our investee companies that might affect the sustainability of their business models. While we do not anticipate any such events, based on our screening of investee companies to date, we will take appropriate action should any occur.

With oil prices rising, some companies might experience increased short-term costs. While this may affect profitability in some cases, we target companies with strong balance sheets that can help them weather challenging economic conditions, as demonstrated during the coronavirus pandemic. We remain confident in the strength of the holdings in terms of solvency and liquidity. We will be monitoring the situation closely, along with our investment advisers Chelverton Asset Management.

Blackfinch Adapt IHT Portfolios

The Blackfinch Adapt IHT Portfolios are split into three companies, Lyell Trading Limited, focused on property development lending, Henslow Trading Limited, focused on asset-backed lending, and Sedgwick Trading Limited, focused on renewable energy generation.

All three companies are designed to target low volatility and stable growth and typically have little to no correlation with short-term movements in listed markets. This has afforded them an element of protection against this current volatility. Additionally, assets in all companies are based in the UK, with no European asset exposure.

Wholesale electricity prices are closely tied to wholesale gas prices, which have risen rapidly in recent months, linked primarily to a demand and supply imbalance as Western economies have rebounded strongly from the coronavirus pandemic. The conflict in Ukraine is likely to exacerbate this imbalance, leading to further upward pressure on gas prices and therefore wholesale electricity prices in the short term, which should be positive for owners of electricity generation assets. Taking a longer-term view, it appears Western European governments must intensify their efforts to reduce their dependence on Russian gas supplies as part of a wider energy security strategy. Such a transition would also be highly beneficial for investments in renewable forms of energy generation, such as wind and solar farms.

Blackfinch Ventures

The conflict in Ukraine has the potential to impact high growth technology companies in several ways, particularly through the disruption of outsourced software development teams located in the region. Ukraine, along with several other Eastern European countries, is home to a growing pool of talented developers. We are in close contact with all our 20+ portfolio companies, and only one has a significant Ukrainian development team. Members of this team are currently relocating to Poland and Lisbon, and we will support the company during this period in any way we can.

Whilst many of our portfolio companies are expanding their customer base internationally, none have significant revenue exposure to customers in Ukraine or Russia. Blackfinch Ventures has purposefully built our portfolio to be resilient, by investing across different sectors, and industries. That level of diversification can give investors some peace of mind in the face of geopolitical events.

Looking forward

In general, a crisis like this will only have a significant and lasting impact on global financial markets if it has a sustained macroeconomic impact on major economies. Therefore, it is important for us to continue to manage those factors within our control on behalf of the investors and financial advisers who place their trust in us.

Richard Cook,

Chief Executive Officer, Blackfinch

IMPORTANT INFORMATION

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