# TERRACAPITAL
## NATURAL RESOURCE FUND

DECEMBER 2018

| | 1M | 3M | 6M | FYTD | 1Y (rolling 12mths) | 3Y (p.a.) | Inception (p.a.) | Inception (cumulative) |
|---|---|---|---|---|---|---|---|---|
| Terra Natural Res. Fund | -7.3% | -18.7% | -27.2% | -27.2% | -36.2% | 18.6% | 17.1% | 283.1% |
| ASX/TSX Composite** | -0.6% | -9.2% | -17.4% | -17.4% | -14.2% | 20.8% | -7.1% | -46.5% |
| ASX Small Resources | -5.1% | -14.5% | -20.3% | -20.3% | -16.0% | 22.7% | -7.2% | -46.9% |
| TSX Mining & Minerals | 12.7% | 7.1% | -9.5% | -9.5% | -9.2% | 16.4% | -6.9% | -45.5% |
| Exit Unit Price | $2.1951 | | | | | | | |

*Terra Capital Natural Resource Fund movements are shown net of (after) fees. Inception: 1st July 2010*
*** ASX/TSX Resource Composite is a weighted average which best fits the mandate. 60% from ASX small resources and 40% TSX mining and minerals*

### Performance & Overview

The Fund returned -7.3% after fees for the month of December 2018. Since inception (July 2010) the Fund has returned +283.1% after fees vs. the ASX Small Resources Accumulation Index -46.9%.

The Unit Price is currently $2.20

### Markets

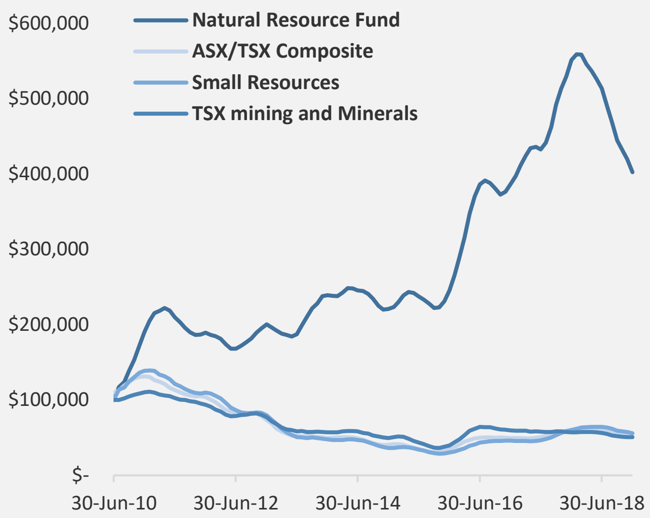
The Australian market had the worst close to the year since 2011, with the S&P/ASX 200 index closing December -0.4% lower. Despite closing in the red, the Australian market outperformed global equities which were impacted by concerns over global economic growth and the potential for a monetary policy misstep by the US Federal Reserve.

Global equity markets continued to remain under pressure as one part of the US yield curve inverted at the beginning of the month. The spread between the 5-year and 3-year yields fell to as low as -4bps, raising further concerns about the outlook for the US economy. The S&P 500 index fell -9.2% and the Nasdaq slid -9.5%.

Market chatter over a potential shift in the US Federal Reserve's guidance at the beginning of the month also spooked equities. These concerns came to fruition with the US Federal Reserve increasing the Fed Funds rate to 2.5%, from 2.25%, but reducing their rate expectations for 2019 to two additional hikes from three, and their long-term expectation to 2.75% from 3%.

Risk assets slid further as fears over the health of US and China relations rekindled following reports that a senior Chinese telecommunications executive had been arrested in Canada on fraud allegations with possible extradition to the US. These events seemingly unwound the positive sentiment following the G20 meeting where Trump and Xi agreed to a ceasefire.

**Value of $100,000 invested at inception**




In Europe, protests in France over the month are likely to impact the economy. Brexit negotiations continue to impact asset prices with both UK bond yields and the British pound falling around mid-month in response to the government's delaying a parliamentary vote on the Brexit deal. Separately, the European Court of Justice ruled that the UK doesn't need the EU's permission to revoke its intention to leave the EU. Intriguingly, this now opens the possibility of a pain-free retreat back to pre-referendum days, if the UK asks for it.

In China, the PBOC cut the funding cost for commercial banks for the first time since February 2016. Asian markets were weaker with the Hang Seng falling -2.5%, the Nikkei moving -10.5% lower, and the SSE Composite index falling -3.6%.

**Commodities**

It was a difficult year for commodities, with markets largely dominated by policy moves including China's on-going industry reforms (capacity cuts and pollution controls), US tariffs on steel/aluminium trade, US sanctions on Rusal + Iran, US-China trade conflict, and OPEC/Russia collective evolving oil production policy.

In December, crude oil prices continued to move lower with WTI falling -11% to US$45/bbl. This is despite OPEC and member countries agreeing to a 1.2mb/d cut, relative to an October baseline. The duration of the deal is six months, with a review in April.

Base metals were mostly lower in December as sentiment in global metal markets weakened despite improved trade dialogue and the 90-day stay of tariff-loading agreed between the US and China at the G20 Summit in Argentina at the beginning of the month. Copper (-5.6%), nickel (-4.9%) and zinc (-3.2%) prices fell whilst lead (+2.2%) was in the black.

Aluminium prices fell 6.5% as the US Office of Foreign Assets Control (OFAC) announced another deadline extension to wrap up business dealings with aluminium giant Rusal and other companies associated with oligarch Oleg Deripaska. This implied that OFAC are reaching the final stages of a deal to allow for sanctions to be lifted. Reports of the US planning to lift sanctions on the Russian producer in 30 days then followed.

Precious metals surged with gold up 4.5% and silver 9.3% higher as investors rotated to safe haven assets. The outlook for gold arguably improved in December as the US Federal Reserve lowered its expectations for 2019, with the prospect for a pause in its hiking cycle. Gold tends to move in the opposite direction to rate expectations.

Iron ore prices surged 10.1% in response to reports that a number of cities in China have eased property market restrictions, boosting expectations for steel demand. Speculation that the country could launch more infrastructure projects in 2019 also supported prices.

**Portfolio commentary**

2018 was a year we wish we could start again. Last year began with global synchronized growth, historically low volatility, bullishness, a ramping US economy, commodity demand and supply dynamics looking the best they had done in over 5 years and the potential for high EPS growth in the US.

We begin 2019 with a global slowdown, high volatility, bearishness, a slowing economy, and the potential for flat US earnings growth.

We believe the Q4 18 market crash, the fourth in the last 40 years, more than discounts the slowing domestic and global economy, as long as the Fed stops making policy and communication mistakes, the Trump Administration resolves the trade conflict with China, and the yield curve remains positive.

The recent comments from Fed Chair Powell at the American Economic Association and recent comments from the Administration did help relieve fears around these issues. All considered we don't believe the outlook for 2019 is as grim as the mainstream media suggests.

The International Monetary Fund recently released figures showing the global economy grew at 3.7 percent in 2018 and the forecast remains a healthy 3.7% for 2019. While we believe that it may take some time for stocks to recover with news from the US-China trade negotiations out soon and Q4 earnings likely to set the short-term direction. Additionally, the Federal Reserve is widely expected to further reduce its current call for another two rate hikes this year.

After seeing slowing growth, we saw stimulus in China via a rail announcement immediately as 2019 got underway:

*"China plans to invest in 6,800 kilometers (4,225 miles) worth of new railway lines in 2019, a 40 percent jump from the length of tracks laid last year, amid a wider push to boost infrastructure spending. At least 3,200 kilometers of this target will be high-speed rail"*.

***Commodities Outlook***

Apart from supply and demand dynamics, the US dollar will play an important role and at this stage we see the risk of further US dollar weakness, although it may take some time to emerge.

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Crude oil has bounced following the +40% collapse since last October. Since hitting the key technical and psychological $50/b level recently it has managed to recover strongly due to an improved outlook for both supply and potentially also demand.

In base metals, Copper dropped every quarter last year in the worst run since 2015. Like many metals, copper was hurt by concerns that global growth is slowing, and the U.S.-China trade fight. A fundamentally supportive backdrop exists though, offered by industrial indicators. Among these are global stockpiles tracked by exchanges, with holdings in London Metal Exchange sheds at a decade-low.

Copper demand topped supply by 595,000 tons in the nine months to September, according to the International Copper Study Group. At the same time miners highlight lower grades.

Just as trade-war swings hurt copper in 2018, the same could be true in 2019 -- but in reverse. Should Washington and Beijing settle some issues, copper could gain. Prices recovered ground recently on confirmation of the talks. The median of forecasts tracked by Bloomberg puts the metal, which was last at $5,930 a metric ton, above $6,400.

Uranium and Nickel are also compelling fundamentally, and support has emerged for a number of commodities after news about next week's resumption of trade talks and China's government pledged to strengthen counter-cyclical economic policies.

To summarise, the negative performance of 2018 was caused predominantly by political events. If the China/US situation improves and the US dollar continues to fall we think equities, and resources in particular will perform well.

While we remain cautious, we are hopeful of a less bumpy road globally in the year ahead that will allow commodity fundamentals to play out.

In our opinion, 2019 begins from the most attractive point in many years in terms of mining and energy stock valuations and we remain aware that timing an equity market recovery is impossible but as the recoveries from 2009 and 2015 and show; you don't want to miss them when they come.

We thank you for your ongoing support and welcome any feedback.

# TerraCapital
## NATURAL RESOURCE FUND

DECEMBER 2018

### Natural Resource Fund Strategy

The Fund is a global, long only mining and energy fund established in July 2010. The Fund's strategy is fundamentally driven, high conviction, high concentration and we pride ourselves on our relationships with our investors. Terra Capital's research driven process and true active management is complimented by a focus on risk management.

The objective of the Fund is to deliver superior absolute returns over the medium to long term by investing in small to medium-sized companies in the mining and resources sectors.

### Fund Details

| | |
|---|---|
| NAV | $2.2006 |
| Entry Price | $2.2061 |
| Exit Price | $2.1951 |
| Fund Size | $54.9M |
| APIR Code | TER001AU |

### Top 5 commodity exposure

| Commodity | % of fund |
|---|---|
| Cobalt | 17% |
| Gold | 16% |
| Base | 14% |
| Other | 13% |
| Lithium | 10% |



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