TERRACAPITAL
NATURAL RESOURCE FUND

DECEMBER 2016

	1M	3M	FYTD	1Y (rolling 12mths)	3Y (p.a.)	Inception (p.a.)	Inception (cumulative)
Terra Natural Res. Fund	1.04%	-13.22%	-10.94%	50.17%	15.60%	20.96%	244.8%
ASX All Ords	4.17%	4.41%	9.94%	11.65%	6.76%	9.02%	75.4%
ASX 300 Mining	2.94%	8.43%	26.97%	56.21%	-0.89%	-2.2%	-13.5%
ASX Small Resources	2.46%	-1.70%	6.31%	59.47%	-0.91%	-11.3%	-54.2%
Unit Price	$2.34						

Terra Capital Natural Resource Fund movements are shown after fees. Inception: 1st July 2010

FUND PERFORMANCE

During the month the ASX 300 Metals and Mining was up 2.9% whilst the ASX Small Resources Index was up 2.5%. The ASX All Ords were up 4.7% for the month. Against this backdrop the Fund was up 1.0%.

The Unit Price is currently $2.34

AUSTRALIAN MARKETS OVERVIEW

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GLOBAL MARKETS OVERVIEW

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Global equity markets rallied strongly on the back of increased optimism that president elect Donald Trump will increase infrastructure spend and cut taxes and as the Energy sector rose strongly off the back of OPEC agreeing to cut production by 3.7% from October levels.

The Dow Jones and S&P 500 were up +3.3% and +2.0% respectively, and Europe and Asia also posted solid gains - German DAX up +7.9%, Euro STOXX +7.1%, the UK FTSE 100 +5.4% and the Japanese Nikkei 225 +4.6%. The US market posted strong annual gains - the Dow Jones rising +13.4% in 2016 as earnings expectations were reset higher in the wake of the US election and as Fed rate hikes did not eventuate as expected keeping bond yields well behaved but for the final quarter of the year.

Global markets took their cue from a strong US with European markets also rallying strongly through the year. The FTSE 100 rose +19.1% (benefiting from a weaker sterling despite BREXIT), German DAX +6.9%, and the Euro STOXX +4.2%. Asian markets had a more roller coaster ride through, generally weak into mid-year before finishing 2H strongly but generally underperforming Europe and US. Hong Kong led major Asian markets rising +4.3% with Japan following up +2.4%.

COMMODITY OVERVIEW

In general, commodities performed well over the quarter and notably, despite the appreciation of the USD. Iron ore was the biggest mover, up 24% Q-on-Q, while base metals also performed well, with copper, zinc and lead all averaging significantly higher prices compared to the September quarter.

Average LME prices for copper, zinc, lead and nickel rose by 11%, 12%, 15% and 5% respectively in the December quarter. Whilst base metal equities performed well, they lagged commodity price rises, up just 5% Q-on-Q.

In 2017, we forecast zinc to perform well and potentially spike above US$3,000/t as a result of smeltered metal deficits declining inventories.

Nickel volatility will likely remain based on Government enforced closures of Philippine laterite mines and the potential restart of some Indonesian laterite mines. With very few copper mines coming on line in 2016, we see good support for prices above US$5,500/t.

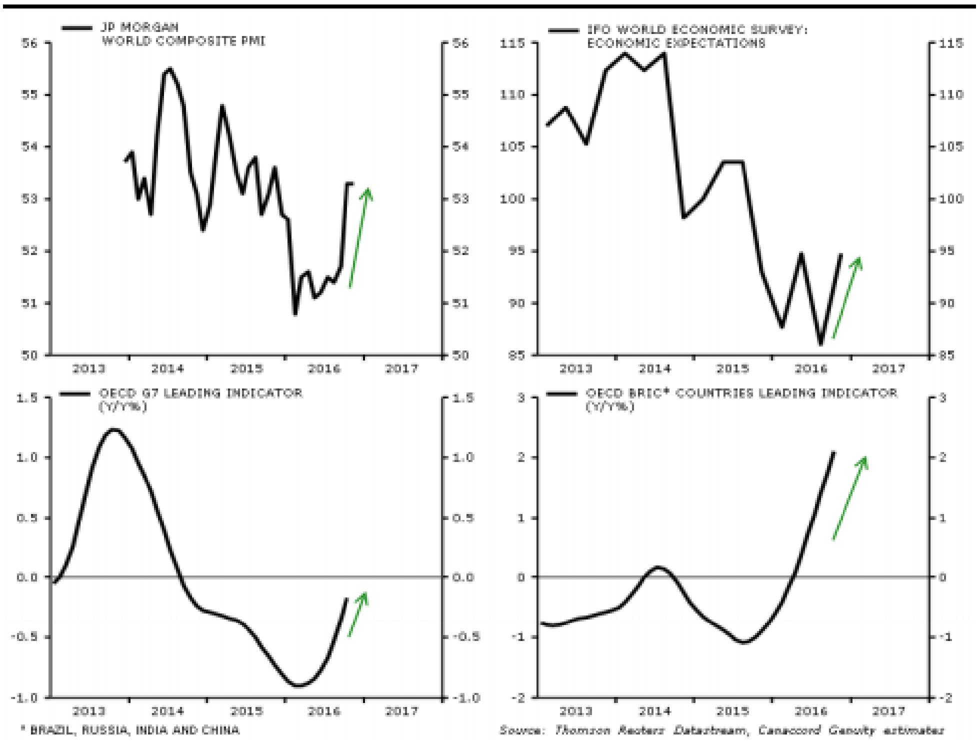
The average gold price declined 11.5% in USD terms and -8.1% in AUD terms during the quarter. Prices fell as the US Federal Reserve hiked interest rates for the second time since 2006 and redemptions impacted gold backed ETFs.

Uranium spot prices fell further during the quarter, down 9% to an average US$20/lb and hitting lows of US$18/lb.

MARKET OUTLOOK

After years of lack lustre economic growth, it appears global growth is set to improve in 2017, as suggested by the OECD Leading Indicator indexes for G7 and BRIC countries. The JPMorgan Global Composite PMI and the IFO World Economic Expectations index are entering 2017 in a strong uptrend (Figure 1). In fact, for the first time since 2006, the global economy could experience a "late-cycle" growth synchronisation between developed and emerging market economies (DMs and EMs, respectively). The IMF pegs global GDP growth at 3.4% (up from 3.1%) for 2017, with EMs expected to account for 78% of world GDP growth.

Figure 1: World economy: all systems go



Source: Company Reports, Canaccord Genuity estimates

Canaccord Genuity pertinently reminds investors that global growth reacceleration does not necessarily imply the outperformance of growth vs. value stocks. In fact, there is a negative correlation as investors pay a premium for growth only when it is scarce. When global growth accelerates, globally geared (i.e., technology and industrials) and resource sectors (energy and materials) usually lead markets. Inflation-sensitive groups, such as REITs and golds, also tend to perform relatively well.

These factors tie into what we think are the major factors that will influence the continued positivity in resources stocks:

1. As indicated in Figure 1; US, Chinese, Eurozone and Emerging Market PMI's are trending upwards together for the first time in nearly 10 years.
2. Resource Co management teams continue to maintain financial discipline post the recent experience of resource sector carnage.
3. Financial discipline has resulted in a significant lack of exploration over the past 5 years. This will lead to scarcity again in the future as demand increases over time and supply response is slower than expected.
4. Impact of reducing inefficient and dirty mines in China – removing supply from the market (as seen recently in coal). Further, Chinese infrastructure spending continues in a number of significant programs.
5. Resource companies remain under-owned in the investment community. This will not remain the case if commodities perform as they did or similarly to what they did in 2016.

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PORTFOLIO OUTLOOK

The gradual repositioning of our portfolio after a highly successful first 7 months of 2016 has us now sitting with what we think present the best opportunities for significant capital growth over the next 6 – 12 months.

While the resources sector did perform well in the December quarter this was driven primarily by large caps with small and mid caps left behind. While this was the case then it rarely remains so and we expect a significant catch up in the months ahead.

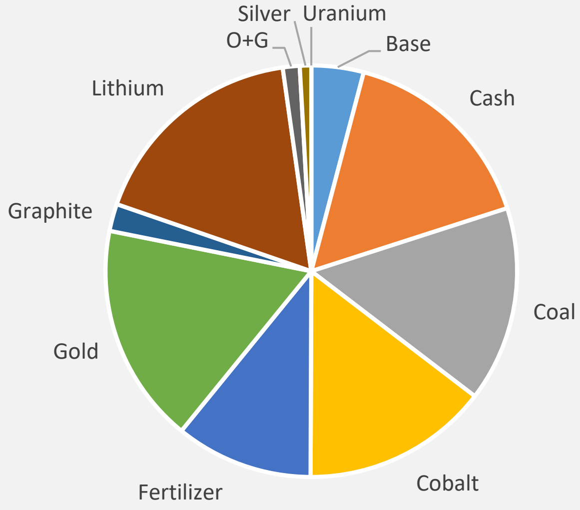
We have retained most of our exposure to gold during the recent commodity price fall which did negatively impact the portfolio during the December quarter but which has had a strong bounce since Christmas.

Having made good money from the electric vehicle theme in 2016 we have repositioned our portfolio to what we think are the best risk adjusted opportunities in lithium, cobalt and graphite. These commodity prices have been exceptional and recent pricing, demand and supply data is all highly positive.

Given the recent positive sentiment towards resource companies combined with the relatively low participation rate in the sector, we are confident in our ability to generate strong returns again in 2017.

We look forward to updating you on our progress and welcome any feedback.

COMMODITY BREAKDOWN



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