

# TERRACAPITAL

## NATURAL RESOURCE FUND

JUNE 2018

	1M	3M	6M	FYTD	1Y (rolling 12mths)	3Y (p.a.)	Inception (p.a.)	Inception (cumulative)
Terra Natural Res. Fund	-3.8%	-3.4%	-12.5%	24.6%	24.6%	25.5%	23.0%	425.5%
ASX All Ords	2.9%	7.7%	4.0%	13.7%	13.7%	9.5%	9.4%	105.3%
ASX 300 Mining	1.5%	14.5%	10.6%	39.6%	39.6%	19.0%	2.5%	21.4%
ASX Small Res.	0.0%	10.4%	5.3%	49.0%	49.0%	23.1%	-5.0%	-33.4%
Unit Price	\$3.0109							

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

### Performance & Overview

The Fund returned -3.8% after fees for the month of June 2018. Since inception (July 2010) the Fund has returned +425.5% after fees vs. the small resources accumulation Index -33.4%.

The Unit Price is currently \$3.01

### Markets

The Australian market (+3.0%) hit a 10-year high in June, rising above the psychological 6,200 level during the month, to outperform global markets in local currency terms.

Currencies that are strongly linked to trade for growth, including the Australian dollar, performed poorly as markets reacted to trade war concerns. The Australian dollar lost -2.2% against the US dollar which likely sparked some offshore interest in Australian equities. Sell-offs in emerging markets also likely drove some inflows into the Australian market.

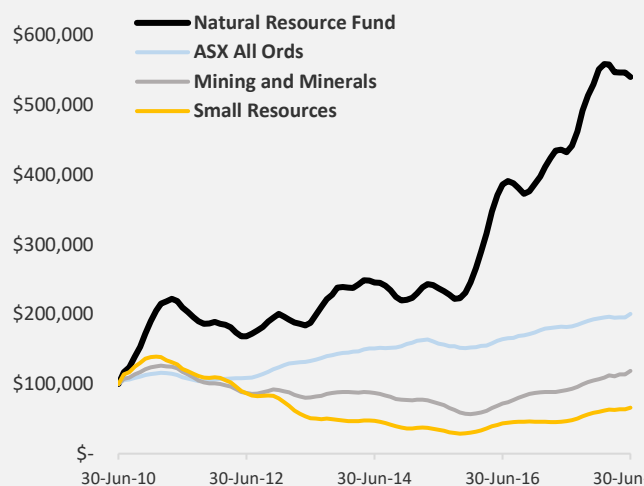
### Commodities

Commodities were weaker in June (with the exception of crude oil) due to concerns over the potential for weaker global growth from an escalation in trade spat originating from the United States.

A firmer US dollar added to the pressure on commodity prices with the US dollar index +0.7% higher in June. Crude oil was the diamond in the rough with WTI rising +10.6% in June to close the month at US\$74/bbl. OPEC held its 174th meeting this month during which member countries agreed to restore group compliance to 100% of the initial 1.2mb/d cut agreed upon in November 2016. It was noted that OPEC member countries have exceeded the required level of conformity, reaching 152% in May. The agreement to

restore compliance to 100% likely means an increase of 0.8mb/d. The price of crude oil was also supported by supply disruptions including the United States' push for all countries to stop importing crude oil from Iran, beginning in November.

### Value of \$100,000 invested at inception



### Portfolio

The Natural Resource Fund finished down 3.8% for the month of June. 2018 has had a lacklustre start for the Fund, down 12.5% YTD, but it has been just as hard for all small mining and minerals companies. Although the small resources index is up 5% since January it's worth noting that resource companies with a market cap of below \$500m were down 7.5% from January 1<sup>st</sup> to June 30<sup>th</sup> (source: Bloomberg).

We are of the view that the small resource market over the past 4 months has been impacted by a combination of tax loss selling and investor fatigue after a solid 2017. As we mentioned in the previous month's report, there is a lag between small resource companies and

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the large caps. The latter has had a fruitful 6 months significantly outperforming their smaller counterparts.

After investors were burnt at the end of the last resources boom, large and mid-cap resource stocks have been returning capital to investors through dividends and share buy backs. This has resulted in limited exploration on new projects and less cash being invested into existing projects. We expect this will lead to an increase in M&A as the large caps look for production growth (which has already been witnessed with Avanco, Mineral Deposits, and Atlas). As commodity prices have increased over the past 12 months we are now seeing cash flows trend in the same direction which should help fund the expected M&A.

The fund's exposure to battery related metals has contributed to our negative performance in 2018 however we believe the sector has been oversold. Our thoughts were echoed by Goldman Sachs in a recent report, the crux of which was that spot lithium prices will stay propped-up by a lack of supply and increased demand over the next 3-4 years.

Further on batteries, Elon Musk publicly announced recently that the Tesla batteries were using less cobalt which negatively impacted equities prices. It's

understandable why battery manufactures are investigating ways to reduce the cobalt content given the current spot price, however the consequence of reduced cobalt is reduced stability and performance. We find it hard to believe that manufacturers and consumers would be happy to forgo battery stability (i.e. increase the risk of catching on fire) for a lower cost alternative which increases the risk of fatalities. Despite Tesla and Elon Musk claiming to have reduced the cobalt content in the Tesla (Panasonic) batteries we look towards the Asian manufactures for industry guidance as they are leading the EV revolution and are still using the conventional 6-2-2 battery with plans to move to 8-1-1 chemistry sometime in the future.

Finally, it's interesting to note that the London Metal Exchange will be increasing its due diligence on cobalt sourced from the DRC, due to the DRC's prolific use of child labour. Given over 60% of the worlds cobalt is produced in the DRC, any push back from the LME should provide a strong tailwind for cobalt projects outside the DRC when the audits start in January 2019. The effects of this could be felt sooner as manufactures look to lock down supply.

# TERRA CAPITAL

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### 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	\$3.0184
Entry Price	\$3.0259
Exit Price	\$3.0109
Fund Size	\$76.9
APIR Code	TER001AU

### Top 5 commodity exposure

Commodity	% of fund
Cobalt	18%
Gold	15%
Lithium	13%
Nickel	10%
Copper	7%

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