# TERRACAPITAL
## NATURAL RESOURCE FUND

JUNE 2016

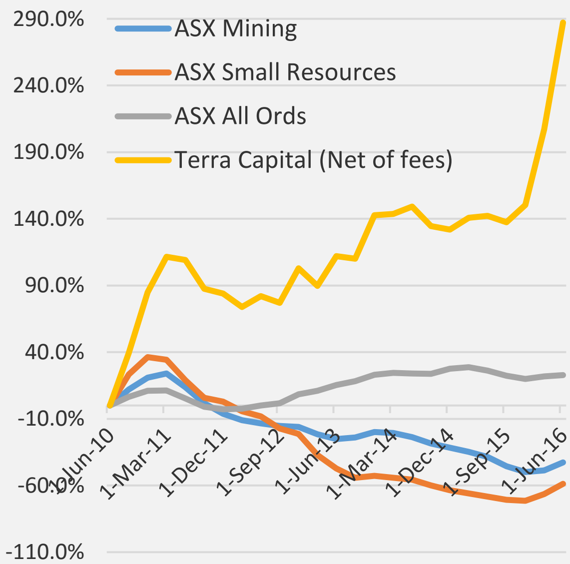
| | 1M | 3M | FYTD | 1Y | 3Y (p.a.) | Inception (annualised) | Inception (cumulative) |
|---|---|---|---|---|---|---|---|
| Terra Natural Res. Fund | 7.3% | 27.2% | 45.7% | 45.7% | 35.0% | 25.3% | 287.2% |
| ASX All Ords | -2.3% | 4.0% | 2.0% | 2.0% | 8.2% | 8.1% | 59.6% |
| ASX 300 Mining | 3.4% | 15.3% | -5.4% | -5.4% | -1.8% | -6.2% | -31.8% |
| ASX Small Resources | 9.1% | 27.9% | 20.7% | 20.7% | 1.1% | -13.1% | -56.9% |
| Unit Price | $2.9123 | | | | | | |

*All Terra figures are shown net of fees*

### FUND PERFORMANCE

During the month the ASX 300 Metals and Mining was up 3.4% and the ASX Small Resources Index jumped 9.1%. The ASX All Ords were lower 2.3% for the month. Against this backdrop the Fund was up 7.3%.

The Unit Price is currently $2.91




### MARKET OVERVIEW

Global markets had a roller coaster ride in June driven by the UK referendum and FOMC's potential stance. The MSCI World index started the month off on a high note in the first week of June as the market priced out the risk of a Fed rate hike in Jun and July on the back of much weaker than expected US non-farm payroll. However this strength was short lived and the index -4% in the following week on heightened uncertainty on the UK referendum (the odds of leaving spiked). This move was reversed mid-month after the Brexit fears faded and after FOMC members unanimously voted to keep rates unchanged at 0.25%-0.5% at the overnight monetary policy meeting, while slightly more dovish comments pushed implied yields from Fed Fund futures and UST yields lower.

The World index had its most pronounced fall (-6%) since Feb as the market comes to terms of the unexpected Brexit vote before recovering some of its losses to end the month -1.1%, which is underpinned by an increasing likelihood of a rate cut in the UK. European markets weakened expectedly on the back of surprise Brexit vote on the 23rd before rebounding almost halfway for both Euro Stoxx and German DAX to end the month down 6%. The most prominent move came from FTSE 100 which has soared in the last few trading days of the month and made its 10 months high +4.7% for June (up 2.8% since Brexit) as Bank of England raised the prospect of a summer stimulus. The pound dropped to a two year low against the Euro -7.7% for the month.

The Emerging markets surged +4.1% for the month as central banks signalled readiness to tackle challenges post the Brexit vote, which has also been a positive driver of the surge in Commodity prices with the Bloomberg Commodity Index up 4.1% for the month.

### COMMODITY OVERVIEW

Base metals turned up during the month with the LME Metals Index rising 4.3%. Notably zinc (+16.3%), nickel (11.3%), aluminium (+8.8%), lead (+5.2%), tin (+2.1%). Copper (-0.8%) declined.

Brent rose 25.5% to $49.68/bbl. Faster declines in mature, high cost, production areas underpin the rebalancing of the market, compounded by outages in Nigeria, Canada and Libya.

Iron ore ended up 3.6% - $55.66/mt. Production cuts from the 'Big 3' (BHP, RIO, and VALE) and a further clamp down on speculative trading in iron ore futures moved the market.

Spot gold increased 7.3% to $1,322. Spot gold reached an intra-day peak just shy of $1,360/oz on the move driven by the uncertainty in the market surrounding Brexit and the Fed's actions over the coming months. Negative bond yields in major economies including Japan, Germany and Switzerland are also supportive for gold. In addition, Chinese purchasing remains strong with net gold imports increasing 80% month-on-month to 3.6Moz in May.

Supply curtailments by the world largest listed uranium supplier Cameco (TSX:CCO) is perhaps the most positive catalyst for uranium prices in the past 12 months. We maintain a bullish medium to long term view with the removal of up to 4.4% of global supply by CCO.

## KEY HOLDINGS COMMENTARY

### NEXGEN ENERGY (NXE.TSX)

The world class nature of Nexgen's Arrow deposit often leads to talk of a takeover. We think that the share price will move higher into 2017 as the resource is increased and we're certainly not pinning our hopes on a deal. A trio of hires at NexGen during June bolsters the Company's management team suggesting the Canadian uranium exploration and development company doesn't need the help of a major to get itself to the next stage. That said it also ensures that NexGen management is well-armed during negotiations with other companies.

Additionally during the quarter Nexgen Energy was able to raise US$60m via an investment from Asia's richest man, Li Ka-Shing. With the proceeds from the convertible (converting at CAD$3.05), NexGen will have approximately $100 million in cash which will provide funding to develop Arrow through permitting.

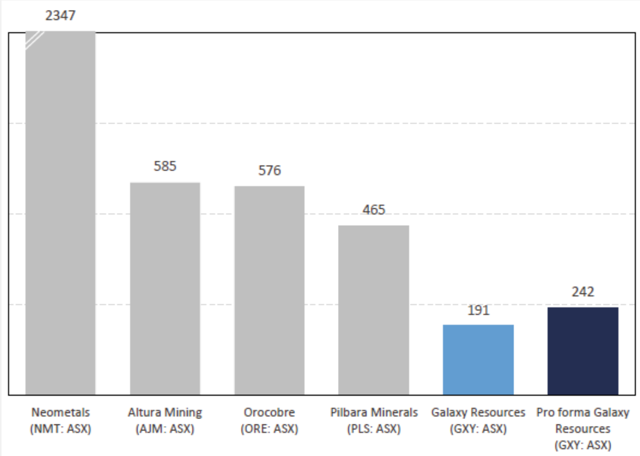
### GALAXY RESOURCES (GXY.ASX)

During June we met Galaxy Resources management to discuss the merger with General Mining. The crux of the conversation revolved around valuation given that the merge Co will be the only ASX pure play lithium company with a portfolio of multiple hard rock deposits and a lithium brine asset (see figure: 1).

For those unfamiliar, brine and hard rock deposits are complimentary when held in a single entity. Established hard rock mines (such as Mt. Cattlin) can be turned on relatively quickly to respond to lithium commodity fluctuations such as the current period where the price has increased. Brine operations – despite being lower cost, cannot alter their output in short time. Brine operations, once commissioned, provide long term, low cost production.

GXY also has the benefit of the cash flow from the Mt Catlin hard rock deposit being available to support the development of the brine asset Sal de Vida. As such we continue to hold a position.

*Figure 1: EV/Resource multiple (A$/t Li2O)*




*Source: IRESS, Bloomberg, company filings*

## OUTLOOK

Another strong month in resources has shown that the pervasive negativity is over and the return to liquidity in mining equities is well underway.

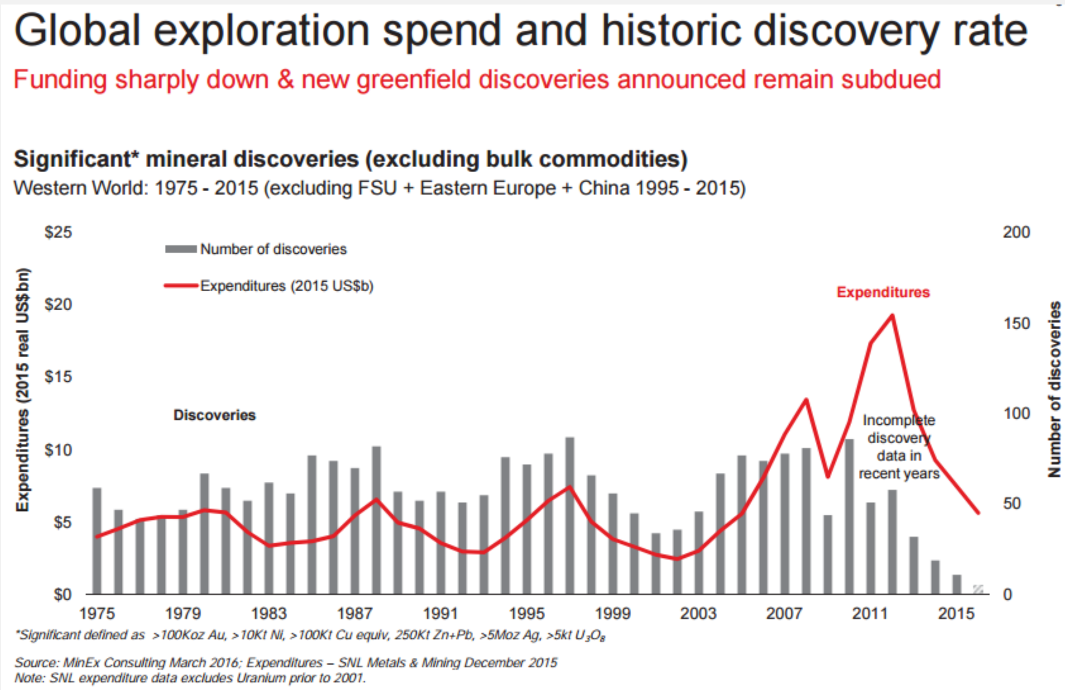
This year miners have outperformed industrials considerably on a year-to-date basis and we're now seeing a few mining shell companies being recapitalised and remaining mining companies rather than morphing into tech or industrial businesses.

We're starting to see (and participate in) some mining IPO's and in specific commodities we're seeing sizeable placements being done. Encouragingly we're also seeing some large offshore institutions participating in stocks where they simply haven't been seen in years. In our experience the offshore funds tend to be amongst the first movers in Aussie mining and energy equities, while domestic generalist funds tend to participate a little later. This is all helping to increase liquidity which of course is very welcome.

As we've touched on in previous reports, costs across the industry have been significantly reduced leading to more compelling feasibility studies and margins. As investors run the ruler over projects these cost reductions mean that projects, particularly in gold stocks, in some cases look extremely compelling.

The following chart (Figure: 2) was presented by Rio Tinto in Sydney on the 27th of June and shows the impact of the downturn mining exploration. This figure shows the number of discoveries, excluding bulk commodities, made across the industry since 1996, along with the estimated worldwide mineral exploration expenditure.

*Figure 2: Rio Tinto*




What we see, is a solid correlation between historic spend and discovery rates through until 2005. Then we see this unparalleled step-up in global expenditure, but without the same anticipated increase in new discoveries.

It should be acknowledged that there will be some backfilling of discoveries in the later years as projects work their way through the evaluation process. However, based on Rio Tinto's analysis, this will add only a minor uplift and, they see no evidence of a large number of new greenfield discoveries coming to market anytime soon.

Over time major discoveries become harder to make and as such, when there's a meaningful dip in exploration expenditure, the pipeline diminishes at a faster rate, in-turn leading to greater commodity price spikes in future. This trend will form the basis of the next bull market in base metals and uranium stocks as we begin to see stockpiles diminish.

We've been utilising the increased liquidity in the fund to our advantage and will continue to do so as more money flows into the sector. We look forward to updating you on our progress on holdings in future.

In Terra Capital news we're adding another staff member as of August and have also increased our number of outsourced analytical and operations staff. In line with best practice, as pioneered by leading funds in the US, our outsourced team who look after unit registry and trade settlement has been complimented by a highly credentialed team that looks after detailed financial modelling and analytics. The group we have engaged and have begun using has incredible capabilities which we look forward to utilising for the benefit of all unit holders.

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