TERRACAPITAL
NATURAL RESOURCE FUND

MARCH 2016

	1M	3M	FYTD	1Y	3Y	Inception (annualised)	Inception (cumulative)
Terra Natural Res. Fund	16.3%	32.6%	14.6%	24.7%	9.9%	21.4%	204.5%
ASX All Ords	4.7%	-2.3%	-1.9%	-8.0%	5.6%	7.7%	53.4%
ASX 300 Mining	6.9%	6.7%	-17.9%	-23.4%	-11.0%	-8.7%	-40.9%
ASX Small Resources	3.0%	17.3%	-5.6%	-5.9%	-20.9%	-17.2%	-66.3%
Unit Price	$2.2907						

FUND PERFORMANCE

During the month the ASX 300 Metals and Mining was up 6.9% and the ASX Small Resources Index jumped 3.0%. The ASX All Ords were up 4.7% for the month. Against this backdrop the Fund was up 16.3%.

The Unit Price is currently $2.29.

MARKET OVERVIEW

What a difference a month makes...or does it? Equities underwent a sizeable rebound through March, rising 4.1% to post the strongest monthly return since October 2015. However, it was not enough to recoup the combined declines suffered through January and February with the ASX200 finishing 1Q16 down 4.0%.

As we have become accustomed, daily price movements were extreme, reflecting shifty sentiment rather than sustained changes in economic or earnings fundamentals. A dovish shift by the Federal Reserve set equities and emerging market risk assets on a higher path into the final day of the month (the ASX200 rose 1.4%) but it was strength in the commodity based sectors – Energy and Materials – that provided the positive platform for the overall market return through March.

Politics remains a talking point with BREXIT and US presidential elections continuing to dominate global headlines; at a domestic level the federal budget has been brought forward by a week, and the Senate has been recalled to consider legislation which could potentially trigger a double dissolution election in July (dismissed by the market without much fanfare or concern); banks led an intra-month sell-off on the back of ANZ's announcement of a worse-than expected resources sector impairment charge.

It was a positive month for global equity markets (MSCI World +6.5%) but with significant dispersion across regions and markets (MSCI Europe +1.0% vs MSCI Asia-X +11.1%).

Latin America was driven by strong local currency and US$ returns from Brazil (Bovespa +17%) as commodity prices and the real appreciated significantly; Asia was led higher by China (SHCOMP +12%), Hong Kong (Hang Seng +9%) and India (Sensex +10%) but its commodity sensitive markets (Indonesia and Malaysia were regional laggards despite a significant weakening in the MYR); Europe was the global laggard (Euro Stoxx +2%) as France (CAC +1%) primarily offset a strong Germany (+5%); the UK was kept in check by ongoing BREXIT concerns (FTSE100 +1%); and the US took a strong lead from the rise in energy equities and later from Yellen's dovish communication that drove both bonds and equities higher (S&P500 +7%).

COMMODITY OVERVIEW

Base metals were up for the month with the LME Metals Index rising 1.1%. Notably tin (+5.8%), copper (+4.2%) and zinc (+1.7%) rose while aluminium (-7.0%), lead (-1.8%) and nickel (-1.2%) declined.

Brent rose 8.8% to $39.8bbl with diminished macro risks, underlying momentum in supply cuts and the prospects of a potential supply agreement delivering the majority of the price recovery.

Iron Ore had an extraordinary surge in early March, rising to $63.7/mt; prices have since retreated to $53.7. Spot gold was among the weakest in the commodities complex; falling 0.1% during March after 2 strong months in January and February.

Address: L12 Domain House, 139 Macquarie Street Sydney NSW 2000 |Phone: +61 2 9252 4293 or +61 2 9252 2518

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Outlook

Another strong month in resources has shown the substantial change in sentiment towards the sector. A realisation has occurred that the best names are relatively cheap and have little downside even at spot prices or slightly below. This realisation is almost impossible to reverse.

The last time resource equities had a run of this ilk was 2011 and since then there has been five hard years for miners and investors in the sector. Commodity prices are well off highs with the realisation that China would at some stage temper it's demand for commodities having long since set in. Falling commodity prices exposed the cost structures of many miners, which had all expanded in step with the price of whatever they produced.

All of that is now history however for the first time since 2011, the first three months of 2016 have been very solid for mining equities. Breaking down the Australian market into key sectors, gold and lithium equities have been the stars of the show, with the Australian Gold Index up circa 28% year to date.

The drivers of this recent rally are fairly clear and thoroughly discussed. Commodities broadly are benefiting from a strengthening US dollar, and gold is seeing interest from investors seeking a safe haven – fearing the prospect of low to negative interest rates for longer, or just possibly the prospect of Donald Trump becoming the President of the United States.

The stand out performance of gold miners has been down to the margins they are enjoying, as they are well ahead of their contemporaries on cost and balance sheet management having been forced into action when the price for gold collapsed in 2013.

As we have discussed in this report previously, gold companies collectively are now exhibiting quite impressive cash generation, driven by low costs and a robust price (especially in many producers currencies). With history as a guide, when rising equity prices line up against increasing cash balances, company aspirations usually shift toward growth, rather than dividends to shareholders. The climate in the gold space looks right for the beginning of balance sheet funded M&A, for several reasons.

1. The largest companies are well funded thanks mostly to their assets producing cash
2. Very few (in Australia at least) have many company changing growth options, most feature various degrees of brownfields extensions. If they want new mines, they are most likely going to have to acquire
3. If big is good, more is better

Of crucial importance is that investors are once again funding fresh raisings of micro-cap miners. This strongly suggests that there has been an immense change of heart – only a few months ago, these stories were judged as too risky for most investors to bother.

The conclusion is not centred on the longevity of the recent rally for miners and commodities – the rally is only an important piece of evidence. It appears that investors broadly have changed their view of miners and the realisations that miners are cheap and probably have very little downside on price, have now set in. The present rally probably won't have the stamina to maintain the impressive returns shown year to date over the longer term, however it appears very clear that capitulation is over, and the beginning of the return of liquidity to mining equities is well underway.

We thank you for your continued support.