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NEDGROUP INVESTMENTS MINING & RESOURCES FUND

Quarter One, 2020

Performance to 31 March 2020	Nedgroup Mining & Resources Fund[1]	ASISA SA Equity Resources & Basic Industries
Q1 2020	-36.1%	-24.8%
12 Month	-23.9%	-20.6%
YTD	-36.1%	-24.8%

Market Commentary

The first quarter of 2020 was completely dominated by the rapid spread of the COVID-19 virus around the globe. Its negative impact made itself felt in every corner of the globe, taking a heavy toll on human lives and economic activity as global lockdowns were implemented. All types of assets, including many traditional safe havens like government bonds, were hit by wholesale selling, which was exacerbated by forced liquidation of many leveraged investors needing urgent liquidity. Uncertainty pervaded investor sentiment as the extent and severity of the virus and its impact on economic growth remained unknown. The IMF warned of a coming global recession worse than that of the 2008 Global Financial Crisis (GFC), while ratings agency Fitch projected a 1.9% contraction in global growth for 2020.

In the US, to counteract the effect of spreading lockdowns across the country, the US Federal Reserve undertook an emergency 100bp interest rate cut and US$700bn in bond buybacks, while the government announced record fiscal stimulus measures to counter the anticipated surge in unemployment and stress on corporate and individual earnings. Markets did not react positively to the Fed's move, with volatility remaining high. Analysts are expecting US GDP growth to contract by around 3.3% for the year, although estimates vary widely.

In the UK and Europe, central banks and governments followed the US's lead, although with interest rates already at record low levels, they were unable to cut interest rates as much. The BoE lowered its base interest rate from 0.75% to 0.25%, and then again to a record-low 0.1% a week later. The ECB established a new 750bn-euro emergency facility to stabilise Eurozone bonds. While both areas announced aggressive fiscal measures, these weaker monetary measures combined with already-lacklustre growth led to fears of worse recessions than the US, with forecasts of -3.9% GDP growth for the UK and -4.2% GDP growth for the EU (by Fitch).

In Japan, the economy was already weak with a much worse-than-expected contraction in GDP growth of -7.1% quarter-to-quarter annualised in Q4 2019, due largely to the impact of the new local consumption tax. With interest rates already at -0.10%, the Bank of Japan left rates on hold but announced a doubling in its purchases of bonds and riskier exchange-traded funds to shore up the economy and markets. However, investors were underwhelmed by the move. Late in March Prime Minister Shinzo Abe unveiled an unprecedented Y60 trillion (US$556 billion) stimulus package to help households and small businesses.

In turn, the Chinese government announced a US$7bn support package for the economy, and the PBoC cut its base interest rate by 20bps. In Wuhan province, the epicentre of the outbreak, and other areas of China, some businesses started to reopen as the worst of the pandemic passed, hopefully pointing to the future of other areas of the globe as well. Analysts estimated Chinese economic growth for 2020 would more than halve to around 2.5% from 5.6% previously.

South African assets and the rand were hit harder by the global sell-off than most emerging markets. This was due to the already-fragile state of the economy, given that it had entered a recession in Q4 2019 with GDP shrinking by 1.4% quarter-to-quarter annualised. Plus, the more liquid nature of the local financial markets made it an easy option for wholesale selling of emerging market risk by global investors amid the flight to safety.

On top of this, government bond and rand sales were exacerbated by Moody's downgrade of the sovereign credit rating to non-investment grade status on 27 March (a move that was widely expected), as well as by the SA government's announcement of some fiscal tax and spending measures to help individuals and small businesses weather the local shutdown, which are expected to push the government budget deficit further into the red. This extra spending rendered February's National Budget plans to reduce the deficit essentially redundant. The extent of the bond sales attributable to the downgrade was unclear, making it difficult to gauge the amount of selling that will come later once South Africa exits the World Government Bond Index of investment-grade bonds. The latter was postponed until after shutdowns are lifted.

Meanwhile, at its 19 March MPC meeting the SA Reserve Bank revised its GDP growth forecast for SA to -0.2% in 2020 from 1.4% previously, which many believed to be optimistic under the current conditions. It also announced a much larger-than-expected 100-basis point reduction in the repo rate to 5.25% in a bid to offer some economic relief. Additionally, it undertook a bond repurchase programme to support the government bond market for the first time. This helped to pare losses in SA bonds.

The price of Brent crude oil was hammered by both expectations of slowing demand and the start of a price war between OPEC and Russia, in which Russia refused to agree with OPEC's demands to lower its production targets to prevent oversupply. The oil price plummeted by 65.6% during the quarter, starting at approximately US$67 per barrel and then hitting a low of under US$25 per barrel before rebounding to end March at around US$34 per barrel.

As for other commodities, only gold and palladium were immune from the Coronavirus sell-off. Gold gained a mere 6.0% for the quarter, despite its safe-haven status, while palladium was up 19.2%. Platinum fell 25.3%. Industrial metals prices, meanwhile, all lost between 17% and 22% as investors factored in a slowdown in global demand until economies recover from the impact of the shutdowns around the world.

Finally, the rand depreciated sharply against all three major currencies amid the coronavirus sell-off, falling 27.4% against the US dollar, 19.5% against the pound sterling and 24.7% versus the euro.

Portfolio Commentary

The fund's top five performing positions added 1.2% to returns over the first quarter while the bottom five detracted -27.3%.

Winners	Ave.weight	Performance Contribution	Losers	Ave.weight	Performance Contribution
Anglogold Ashanti	4.0%	0.5%	Impala Platinum	15.8%	-9.3%
BHP Group	7.2%	0.3%	Sasol	6.5%	-7.4%
Mondi	0.3%	0.2%	Northam	6.3%	-3.7%
New Gold Platinum ETF	0.1%	0.2%	Sibanye Stillwater	9.4%	-3.6%
Textainer Group	0.0%	0.0%	Anglo American	19.6%	-3.3%
		1.2%			**-27.3%**

Current positioning and outlook

The evolving COVID-19 threat had a significant impact on the Platinum Group Metals (PGMs) and oil sectors, even the gold equities struggled to perform during the initial market correction.

Within the PGM sector, palladium and rhodium had been significant beneficiaries of the combination of extended market deficits, rising loadings in autocatalysts as emission standards tightened especially in China, and the inability of a supply response within the broader industry (miners, recyclers, inventory). The only reasonable scenario able to disrupt this confluence of positive drivers was a global recession led collapse in automobile volumes, well above the soft volumes of 2019. The current period of demand and supply disruption creates uncertainty, as quarantined mines complicate the demand recession, but the medium-term fundamentals support a re-tightening of the markets as vehicle volumes recover and emission standards remain a focus. We built small new positions in the platinum and rhodium ETFs and trimmed Impala Platinum.

Oil supply and demand had been running a tenuous balance since 2018 as demand continued its steady froth of 1-2mmbbl/day each year (since the GFC), but the resurgent growth in US shale production of c.2mml/day each year forced OPEC into loss of market share as it took responsibility to balance the market. This supported prices above $50/bbl until demand started to weaken with the initial onset of COVID-19 in China. Subsequently, demand crashed, and Saudi Arabia and Russia failed to agree on a support mechanism and the oil price fell to $20/bbl.

The Sasol share price has been a key casualty of this as the oil price fell below its break-even price, but specifically due to the elevated debt level associated with the LCCP in the US. The company has developed a strategy to deal with the financial squeeze that is likely to involve cost-cutting, asset disposals, debt covenant relief, and equity capital raising. This period of weak oil prices will be testing for the business but see significantly more value in the share when earnings normalise and from the value of the hard assets within the business (well above the lows of c.0.25 P/B).

While gold bullion provided some relative defensiveness during the general equity correction, gold equities provided less protection. The outperformance of gold vs other commodities and the weakness in the rand does provide an attractive valuation underpin for the South African gold miners. We switched the holding in Harmony Gold into DRDGold as we view the latter as less operationally challenged in a period of quarantine uncertainty likely to disadvantage the deep level, labour intensive, conventional miners. We also added to Pan African Resources and funded more Gold Fields by exiting our position in Zambezi Platinum.

During the quarter we also trimmed positions in Anglo American, BHP Group, Glencore and exited Textainer Group that we had inherited from the unbundling from Trencor which we added to, as well as to African Rainbow Minerals.

Responsible Investing

During the quarter we engaged with Exxaro Resources on their strategic shift away from water, energy, and food, to focus on energy – coal and renewables. Broadly we support this initiative as it provides an avenue of corporate growth and life beyond fossil fuels but remains broadly within their area of competence.

Disclaimer

WHO WE ARE
Nedgroup Collective Investments (RF) Proprietary Limited is an authorised Collective Investment Scheme and the representative of Nedgroup Investments Funds PLC in terms of the Collective Investment Schemes Control Act. It is a member of the Association of Savings & Investment South Africa (ASISA)..

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HOW ARE OUR FUNDS PRICED
Funds are valued daily at 15:00. Instructions must reach us before 14:00 (12:00 for Nedgroup Money Market Fund) to ensure same day value. Prices are published daily on our website and in selected major newspapers.

FEES
A schedule of fees and charges is available on request from Nedgroup Investments. One can also obtain additional information on Nedgroup Investments products on our website.

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Some funds may hold foreign securities including foreign CIS funds. As a result, the fund may face material risks, which could include foreign exchange risks, market conditions and macro-economic and political conditions.

A fund of funds may only invest in other funds, and a feeder fund may only invest in another single fund, both will have funds that levy their own charges, which could result in a higher fee structure.

The Nedgroup Investments Money Market Fund offering aims to maintain a constant price of 100 cents per unit. A money market fund is not a bank deposit. The total return to the investor is made up of interest received and any gain or loss made on any particular instrument held. In most cases the return will merely have the effect of increasing or decreasing the daily yield, but in an extreme case it can have the effect of a capital loss. Excessive withdrawals from the fund may place the fund under liquidity pressures and that in such circumstances a process of ring-fencing of withdrawal instructions and managed pay-outs over time may be followed. The yield is calculated using an annualised seven day rolling average as at the relevant dates provided for in the fund fact sheet. Nedgroup Investments has the right to close its funds to new investors in order to manage it more efficiently.

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