NEDGROUP INVESTMENTS

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NEDGROUP INVESTMENTS MINING & RESOURCES FUND

Quarter Two, 2022

Nedgroup Investments Mining & Resources Fund

Commentary produced in conjunction with sub-investment manager, M&G Investments.

Total return as at: 30 June 2022	Fund[1]	Peer Group [2]
3 Months	-10.5%	-15.3%
6 Months	8.2%	1.0%
12 Months	31.0%	21.7%
3 Years	30.0%	21.4%

1. Nedgroup Investments Mining & Resources Fund, A class.
2. ASISA South Africa Equity Resources category

Market Commentary

Investor concerns over a significant slowdown in global growth and corporate earnings escalated during the second quarter (Q2) of 2022. This came as steep interest rate hikes in the US, strict Chinese Covid-19 lockdowns, and the ongoing destructive Russia-Ukraine war led to downward revisions in economic growth expectations for the world's biggest economies. Further rises in energy and food prices led to more speculation over extended inflationary pressures, stagflation, and recession, even as other commodity prices lost ground. This combination of factors resulted in losses across most financial markets – equities, nominal bonds and inflation-linked bonds.

South Africa's fragile economic recovery came under increasing pressure in Q2: growth prospects took a downturn due to the renewal of national Stage 4-6 load-shedding, severe flooding in KwaZulu Natal, rising inflation and higher-than-expected interest rate hikes, as well as the retreat in commodity prices. The South African Reserve Bank (SARB) lowered its GDP growth forecast for 2022 to 1.7% from 2.0% previously. With CPI rising to 6.5% y/y in May – the first time since January 2017 that it has broken through the upper limit of the SARB's 3%-6% target range – the SARB hiked the repo rate by 50bps at its May meeting to 4.75%. The Bank is widely expected to hike by another 100bps at a minimum this year to fight inflation and keep our interest rate differential versus the US as high as possible to avoid more pressure on the rand and SA bond yields.

In the US, inflation hit 8.6% y/y in May, the highest since 1981 and above market forecasts of 8.3% y/y. At the same time, US economic growth shrank by 1.6% y/y in Q1 2022 as consumer incomes and corporate profits were hit by higher prices for food and energy and the end of Covid-related stimulus payments. The US Federal Reserve's 75bp rate hike in June was an aggressive response to this accelerating inflation, a move which prompted more market watchers to predict a recession. Many noted that, given that inflation has primarily stemmed from supply-side factors, higher interest rates were not likely to be as effective in curbing inflation as with demand-driven elements. Fed policymakers now see rates reaching 3.4% in 2022, well above the 1.9% forecast in March, and increased chances of recession.

Chinese investors became more upbeat towards the end of the quarter as Covid infection rates started to slow, allowing the government to ease some of its ultra-strict lockdown conditions in Shanghai and certain other areas. The country recorded better-than-expected GDP growth of 4.8% y/y in Q1, up from 4.0% y/y the previous quarter. The latest data showed a surge in manufacturing and non-manufacturing PMI in June, accelerating to 51.7 (up from 48.1) and 54.7 (up from 47.8), respectively. The People's Bank of China (PBOC) left interest rates unchanged at its June meeting, in line with expectations. The Central Bank is concerned not only about growth but also about the widening divergence between local and US interest rates, which has put Chinese bonds and the yuan under selling pressure.

Energy prices continued their rise, but at a moderated pace: Brent crude oil gained 6.4% during the quarter after experiencing some softness in June. Year-to-date, the price is up some 47% in US dollars. In precious metals, gold fell 6.0% for the quarter, platinum lost 7.7%, and palladium was down 13.2%. Other industrial metals prices lost between 20-30% amid heightened worries of a global growth slowdown.

The FTSE/JSE All Share Index (ALSI) returned -11.7% for the quarter and the Capped SWIX -10.6%, dragged down by Resources with a -21.9% return, -15.8% from Financials, -12.1% from Listed Property (All Property Index) and -3.0% from Industrials. For the six months of 2022, the ALSI has returned -8.3%, outperforming the -18.2% recorded by global equities (the MSCI All Country World Index) in rand terms.

Portfolio Commentary

The fund's top five performing positions added 3.09% to returns over the quarter, while the bottom five detracted -9.45%.

Winners	Ave. Weight	Performance Contribution	Losers	Ave. Weight	Performance Contribution
Thungela Resources	8.39%	2.66%	Anglo American	15.94%	-3.88%
Sasol	11.16%	0.48%	Northam Platinum	7.72%	-1.59%
New Gold ETF	0.58%	0.02%	Gold Fields	4.79%	-1.42%
Cash	1.88%	0.01%	Impala Platinum	7.76%	-1.42%
BHP Group	1.40%	-0.07%	South32	4.39%	-1.14%
		3.09%			**-9.45%**

Current positioning and outlook

Structurally we remain constructive commodities, principally due to rising supply constraints of regulation, ESG and constrained investment, and metals intensity of the energy transition. However, cyclically, the headwinds have increased during Q2, as the markets weigh up the extent of the economic slowdown and risk of recession, as the global monetary conditions tighten around rising inflation concern. In addition, Chinese Covid lockdowns and Russia's war in Ukraine, added uncertainty.

We can observe the cyclical contraction in the OECD leading indicator, an essential series followed by commodity economists, which has been declining for a year but dropped below 100 in Q2, signalling contraction. Commodity market tightness does not appear to have evaporated to the extent that prices have fallen. Energy markets remain tight, and base metal inventories are low, but financial markets have swung against the sector as it attempts to pre-empt a soft or hard landing for the global economy.

Commodity prices remain at healthy premiums to the marginal cost of supply. This indicates that price tension is still in place from constrained supply and that mining companies still have healthy margins. However, it also indicates that despite price weakness in Q2, commodity prices have further to fall if economic conditions drive commodity markets into surplus and require supply rationing.

So we have the dilemma that equity margins and free cash flow are healthy, and valuation multiples are optically attractive. Still, sequential earnings momentum and consensus earnings revisions are turning down and represent a substantial drag on equity performance. So the depth and duration of a looming contraction are critical to positioning.

We prefer energy-related commodities, oil and coal within a South African portfolio, and defensive non-mining basic materials. We remain cautious on iron ore and platinum group metals. While gold, we acknowledge, still offers a favourable defensive role, and we are positioned accordingly, we note that the South African gold equities provide a weaker safe-haven characteristic than bullion.

China remains a wild card. We believe the balance of market forces for commodity markets has shifted from China to global macro, but still see China as singularly important. Over the past decade, Chinese credit conditions have been a powerful driver of commodity cycles. However, the combination of a zero-Covid policy and an over-reliance on the property market as a primary driver of Chinese growth, appears to weigh against this as a lever. Infrastructure investment currently seems to be the preferred lever but follow through into the real economy and commodity demand is yet to be seen.

During the past quarter,

- We took profit on our thermal coal positions (Thungela and Exxaro).
- We reduced our significant Anglo American position, adding to BHP for its high quality, despite our caution on iron ore as a commodity, and South32.
- In the gold sector, we reduced our position in Gold Fields following a review of its re-rating. Later, the company announced its intent to take over Canadian listed Yamana gold in an all-share offer.
- In addition, we increased our position in Pan African Resources, which we view as the discount rated SA gold miner, and we created a position in New Gold ETF, our preferred defensive/safe-haven asset.
- In the platinum sector, we switched some Impala Platinum into Northam Platinum.
- We also added to Sappi, favouring non-mining over mining equities in the current cycle.

Responsible Investing

On the governance side, we engaged mainly around remuneration during the quarter. Most notably, Northam and Sasol stood out.

Sasol has made substantial strides in its remuneration policy structure and provisions in recent years. As a result, the current discussions were around metrics, measurement and finer details.

Northam is still refining its remuneration structure, and here our focus has been around engaging broader governance provisions and principles that we wish to see included.

On the environmental front, two engagements were of interest and worth mentioning.

Thungela was engaged around its total potential carbon output and on acid mine water leakage into a river system. The latter is interesting as illegal miners' actions seem to have triggered the environmental damage at a mine no longer under production. Thungela has been struggling with local law enforcement to remove illegal miners. The illegal miners are operating significantly under the blind eyes of authorities, yet the mine owner bears the liability for the environmental damage they cause.

At **Glencore**, we have engaged in their coal policy objectives and climate policy timelines. This helps us understand the difficulties mines face in responsibly working down the existing coal assets, ceasing operations (and risking a loss of licence) and the implications of selling these assets to other parties, including private equity, who may not be accountable to public shareholders. We also engaged Glencore on aspects of its climate policy resolutions that may be tabled at its next AGM.

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)..

OUR TRUSTEE
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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.

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