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NEDGROUP INVESTMENTS MINING & RESOURCES FUND

Quarter Four, 2022

Nedgroup Investments Mining & Resources Fund

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

Total return as at: 31 December 2022	Fund[1]	Peer Group [2]
3 Months	11.3%	13.6%
6 Months	12.0%	12.5%
12 Months	21.1%	13.7%
3 Years	27.2%	24.9%

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

Market Commentary

In the final quarter (Q4) of 2022, global financial markets recovered some ground lost during the past three quarters that were dominated by bearish sentiment and negative news. Although the outlook remained gloomy, some light emerged. In October and November, buyers were attracted by cheaper asset valuations and somewhat improved clarity on company earnings prospects, as well as falling fuel and food prices. By mid-December, an easing pace of the interest rate hiking cycle added to the better sentiment. However, caution returned in December: still causing uncertainty were unknowns such as the severity of the expected 2023 global growth slowdown, the impact of the massive new Covid wave in China, the ongoing tragedies of the Ukraine-Russia war, and the stickiness of inflation in large economies. As such, markets retraced some of their earlier gains in December.

Key central banks like the Bank of England and European Central Bank (ECB) followed the US Federal Reserve's lead during the quarter, each hiking interest rates by 75bps in November and 50bps in December – the latter a sign of some slowing in the upward trajectory. However, these banks also indicated rates were likely to remain higher for longer than expected given their tough inflation stances and signs that inflation was becoming more pervasive, including rising services costs and wages. Each acknowledged the negative consequences for economic growth in 2023.

In South Africa, the SARB also matched the Fed's 75bp rate hike in November and is expected to follow its 50bp increase in January. Despite continued load-shedding and a spike in political risk in early December on reports that President Cyril Ramaphosa might resign, local equities and bonds benefitted from the more optimistic investor sentiment, outperforming the major global indices. The FTSE/JSE All Share Index (ALSI) returned 15.2% in Q4. Listed Property shares were the strongest performers with an 18.2% return (All Property Index), followed by Resources with 17.6% (Resources 10 Index), Industrials (15.7%) and Financials (11.9%).

After rising 3.2% y/y in Q3 on the back of surprisingly strong consumer spending, US economic growth for all of 2022 is forecast at around 1.9% before slowing to below 1% for 2023. Data showed that the US housing market is already slowing meaningfully and is expected to be a significant factor in the slowdown. However, consensus projections are for a relatively mild and brief recession lasting for the first three quarters of next year.

In the UK, new Prime Minister Rishi Sunak's sweeping new budget plan was greeted more favourably than Liz Truss's disastrous September mini-budget, proposing higher taxes and lower spending to reduce the government's substantial debt levels.

The ECB followed the US Fed and BoE with its 50bp hike in December after a 75bps increase in late October while suggesting similar-size hikes at its next two meetings. Eurozone inflation fell to 10.1% y/y in November from a record 10.6% as energy costs eased. However, the ECB still expects a short and shallow recession in 2023 as the energy crisis is seen weighing heavily in the shorter term while the Ukraine-Russia war drags on: it downgraded the region's GDP growth to 0.5% in 2023 (from 0.9% previously), while in 2024 it is still projected at 1.9%.

In Japan, the Bank of Japan (BOJ) surprised markets in mid-December with its first effective interest rate hike, raising its 10-year bond yield range by 0.25% to 0.50% after long periods of stability. This triggered equity and bond losses globally over fears that Japanese investors could start moving to hold more Japanese bonds by selling their extensive holdings of US Treasuries. It also sparked a 3% gain in the yen on the day. The market had been pricing in no rate increases through 2023. Finally, the BOJ revised its real growth outlook downward for 2022 to 2.0% from 2.4% previously and for 2023 to 1.9% from 2.0%, but no recession is expected.

In China, it was a chaotic end to the year as the government responded to widespread social protests against its strict zero-Covid policy by removing almost all restrictions. However, this came as a new wave of Covid infections was spreading, with some projections that it could result in upwards of 1.0 million deaths, given the population's vulnerability and fears that it would spread widely during the Chinese New Year travel period. Although economists welcomed the move to help free up the economy and kick-start growth, the uncertain impact of the virus weighed negatively on markets. Ongoing property market weakness also undercut consumer and business sentiment. Meanwhile, consensus forecasts for China's economy call for only 3.3% GDP growth in 2022, far below the government's 5.5% target and the slowest since the 1970s. For 2023, a new government target of 4.5%-5% is reported to be most likely, but many consider this optimistic.

Thanks to the renewed global risk-on sentiment, the final months of 2022 proved better for South African investors, despite the elevated market volatility. Our local equity and bond returns outperformed global market benchmarks in Q4. SA bonds and the rand even fully recovered their losses from the 1-2 December market sell-off prompted by reports that President Ramaphosa was considering resigning over the Phala Phala scandal. At the party's mid-December elective conference, ANC members rallied behind him, and he emerged even stronger than before, with more ANC Executive Committee members supporting his economic reform agenda. This helped lower political risk premia on SA assets.

Also, in more positive news, November's CPI fell to 7.4% y/y from 7.6% in October, primarily attributable to lower energy prices: the SARB forecast it to reach the 4.5% mid-point of its target range by Q2 2024. Equally positive was that Q3 real GDP growth surprised to the upside at 1.6% (q/q annualised), primarily led by higher agricultural production. By the end of the period, the size of the SA economy had finally exceeded pre-pandemic levels. However, in its Medium-Term Budget, the National Treasury lowered its growth expectations for 2022 to 1.9% (versus 2.1% previously) and 2023 to 1.4% from 1.6%. The SARB's latest projection was for 1.8% GDP growth in 2022. This was due to still-elevated inflation, rising interest rates, subdued consumer demand and slower economic growth, the war in Ukraine and the impact of load shedding: in its December Quarterly Bulletin, the SARB estimated that Q3 real GDP growth (quarterly) had likely been reduced by 2.3 percentage points due to the high intensity of power cuts. For the year to the end of October, it said, load-shedding had occurred 33.4% of the time or an average of 10.4 calendar days per month.

The oil price fell during the quarter because of expected lower demand and improved supply, even though some supply cuts came from Russia in December. Brent crude oil lost 2.3% in US$, ending the quarter at around US$83 per barrel. Over the past 12 months, the oil price has been only 10.5% higher. Other commodity prices gained ground in Q4 amid the more positive sentiment, apart from palladium, which fell 17.2% after gaining in the previous quarter. Among precious metals, gold rose 9.8%, and platinum jumped 24.1%. Nickel was the strongest gainer in industrial metals at +36.5%, lead was up 23.6%, aluminium rose 8.3%, copper increased 9.7%, and zinc was up only 1.3% in Q4.

Portfolio Commentary

The fund's top five performing positions added 10.30% to returns over the quarter, while the bottom five detracted -1.63%.

Contributors	Ave. Weight	Performance Contribution	Detractors	Ave. Weight	Performance Contribution
Anglo American	14.23%	2.94%	Thungela	5.74%	-1.04%
Glencore	12.56%	2.58%	Sasol	10.17%	-0.41%
Impala Platinum	8.79%	2.11%	Omnia	3.77%	-0.17%
Northam Platinum	8.54%	1.55%	PPC	0.98%	-0.05%
Anglogold Ashanti	3.42%	1.12%	Orion Minerals	0.35%	0.04%
		10.30%			**-1.63%**

Current positioning and outlook

The complex interaction of multiple risk factors, offset with evolving multi-decade trends (specifically, within our mandate, in energy security and transition, as well as supply constraint), requires a balance of defensiveness and risk-taking within the fund. If we had known the global events of the past three years ahead of time, we may have reduced our risk appetite and sacrificed returns. By predominantly taking a bottom-up approach to stock picking, we identified the health of the JSE resources sector, specifically in cash flow generation, supported by balance sheet strength and capital discipline, thus providing strong shareholder returns.

Cross-sector market risk also needs to be managed carefully as upward squeezes in commodity prices are apt to emerge (as are air pockets). While we actively monitor macro outcomes and apply a thread to our positioning, our primary energy is spent correctly picking stocks within subsectors and matching risk within our constrained JSE resource universe.

Near-term uncertainties that we consider into 2023 are China re-opening and its ability/appetite to stimulate the economy, mainly through the property sector, as well as slowing global growth, inflation and interest rates, reflected in recession risk across the globe (the soft or hard landing debate).

The long-term underpin remains the energy security challenge of 2022 evolving into a clean energy transition, electrification and decarbonisation, with supply constraints and scarcity, offsetting diminishing contribution from the Chinese property sector to incremental commodity demand (the mega-trend of the past two decades).

In 2022 fossil fuels have been a beneficiary of underinvestment and shutting Russia out of global supply. Iron ore is heavily exposed to China and within China to property – reopening may provide some relief. Still, Chinese property is likely a decreasing driver of commodities well into the future, and this demand will transition into steel intensity of the energy transition and global infrastructure spending.

Commodity scarcity and supply constraints will result in squeezes (as we have seen with Palladium / Rhodium, Lithium / Cobalt, Nat Gas/LNG, and Coal), creating good support for long-life assets. Copper is anticipated to be a commodity in deficit in 2025-2030, but other contenders abound. Beyond identifying these opportunities, the South African investors' challenge is finding exposure within a JSE-listed mandate.

Many commodities (incl gold) are tracking above what we expect at this point in the economic cycle. This may be supported by scarcity and unusually low inventories (reflected in healthy cash flow yields for the miners), but a further demand shock could test this support.

Over the past three months, we have materially reduced positions in Exxaro and Thungela to reflect the strong performance of thermal coal earlier in the year and the improved energy position in Europe, regarding storage levels and a warmer winter. We also exited South32 as its two primary commodities experienced some pressure. The more considerable additions we made were to BHP Group and African Rainbow Minerals, both within general miners to increase exposure to iron ore on account of the opening up of China, DRDGOLD (new position) and AngloGold Ashanti, to raise exposure to gold as the headwind of stronger US$ and rising interest rates wanes, as well as Sappi and Sibanye Stillwater that were added on attractive valuation metrics.

Responsible Investing

In the fourth quarter, our ESG engagements were focused on Sasol and Glencore. We met with all the resource companies under coverage in the previous quarter.

We had a meeting with Sasol's Safety, Social and Ethics committee Chair and members of management, where we discussed the journey of decarbonisation and the sustainability of the business. Since Sasol is a high-carbon emitter, it is essential to have frequent discussions with the company.

We also attended a Sasol Climate change round table where the company committed to the decarbonisation journey and highlighted the work done over the last 12 months.

We also had a governance call with Glencore's Chairman, and specific discussions were held on the company's coal portfolio and the work done on corporate governance.

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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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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