The fund returned 7.7% for the 2018 calendar year compared against a benchmark return of 15.5%. The long-term track record of the fund remains compelling, with it performing well against both its peer group and the benchmark over meaningful periods.

Key contributors to performance in 2018 were our overweight position in Impala Platinum and our underweight position in the gold shares. An underweight position in BHP Billiton, as well as overweight positions in Northam Platinum and Omnia detracted.

During the fourth quarter of 2018, we reduced the fund's holdings in Impala Platinum and BHP Billiton. In turn, we added to holdings in Sasol and Mondi, and initiated a new position in Glencore.

Glencore is a globally-diversified mining company. It produces copper, cobalt, nickel, coal and several other commodities. What makes Glencore unique compared to its peers is its high staff ownership and large commodity trading division. We like Glencore's commodity exposure, which is benefitting from a shift towards electric drivetrains. Glencore's assets are generally low cost and long lived. The company's share price has come under pressure after the US Department of Justice announced that they were investigating the company's activities in the Democratic Republic of the Congo (DRC), Venezuela and Nigeria. Of these, the DRC is the most material, with the country housing Glencore's interests in copper and cobalt via the Katanga and Mutanda assets. We apply a materially haircut to our fair value of Glencore's assets in the DRC and penalise the overall valuation multiple applied to the group to cater for governance risks. Despite this, we still find meaningful upside to our estimate of fair value in Glencore, and feel a small position is warranted.

Looking back on 2018, while it turned out to be a reasonable year for share prices, it was fairly tepid for most commodity prices, despite a promising start. In general, bulk commodities such as coal and iron ore held up and were roughly flat over the last 12 months. Base metals, on the other hand, saw prices come off more meaningfully. Copper was 21% lower, while nickel was 14% lower. It is quite possible that base metals took further pain, given a more liquid financial market (short sellers of commodities use base metals to express a negative view on commodities). Given that base metal markets appear tight, with favorable supply/demand balances and reducing stock levels, this does seem plausible.

Looking forward over the longer term, we remain of the view that commodity markets are fairly tight. Supply discipline from the previous cycle remains intact. Environmental regulation in China is increasing the demand for seaborne tons. While trade wars and a slowing Chinese economy does pose risks, it appears the Chinese government stimulus programme should go some way to offset this, although the time lag from stimulus introduction to real-world impact means we could experience softness in the short to medium term. We remain more constructive on base commodities (vs bulk commodities), given better supply/demand dynamics and better cost curve support.

Portfolio manager
Nicholas Stein
as at 31 December 2018