

The resources sector had a very strong third quarter. The fund returned 9.1%, while the benchmark returned 5.2%. The long-term track record of the fund remains compelling, with the fund performing well against both its peer group and the benchmark over most meaningful periods.

Over the last quarter, the fund benefitted from overweight holdings in Exxaro and the platinum group metals stocks. Overweight holdings in Trencor and Omnia detracted.

During the quarter, we added to our holdings in Anglo American and BHP Billiton. We reduced holdings in Sappi, Mondi, Exxaro and the Platinum Exchange Traded Fund.

BHP Billiton owns large, low-cost assets in iron ore, copper, oil and coal. As a result of healthy commodity prices, combined with restrained capital expenditure (miners still bear the scars from the last down cycle), we expect BHP Billiton to generate meaningful free cash flow in the coming years. We expect a material portion of this will be returned to shareholders, along with the proceeds of their shale gas asset disposal.

News flow over the quarter was dominated by trade wars and, locally, the Mining Charter. The threat of trade wars caused some worry around commodity trade and commodity prices. Our view is that the long-term impact is unlikely to be too material, especially for commodities capable of being rerouted, which is generally the case. Factors such as global population growth and urbanisation are likely to have a greater impact on demand.

The Mining Charter has seen a further revision. This revision is more palatable than the previous iterations, although concerns do remain. On the positive side, the “once empowered, always empowered” rule has been confirmed and the requirement to top up BEE ownership from 26% to 30% for existing mining rights has been removed. For new mining rights, changing the 10% free carry for employees and communities to a 10% carried interest, as well as the removal of a 1% of EBITDA trickle dividend is a positive. The removal of ownership requirements on prospecting rights should aid exploration activity. On the negative side, applying the more onerous new mining rights criteria when assets are sold or renewed, will possibly act as an impediment to new investment and mergers and acquisition activity. Procurement targets remain onerous and will add to the cost of mining.

While the external environment is challenging, we strive to ignore this and remain committed to our disciplined, valuation-driven approach to stock picking and portfolio construction. We still think the resources sector remains attractive, with reasonable upside in most of the stocks within the portfolio.

Portfolio manager
Nicholas Stein

as at 30 September 2018