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WS AMATI STRATEGIC METALS FUND

Quarterly Review

June 2024

By
Georges Lequime, Fund Manager

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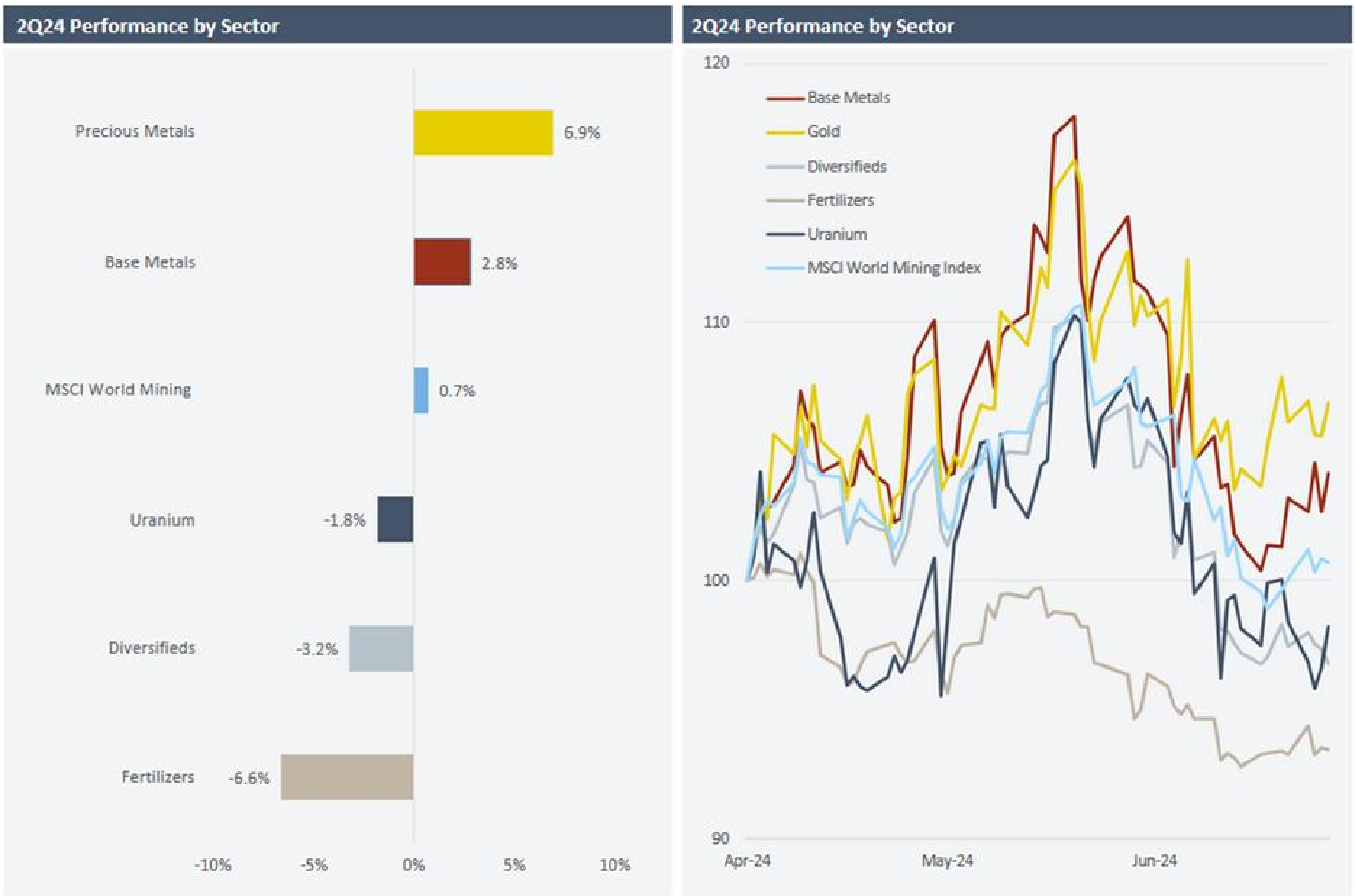
Overall, the second quarter of 2024 proved to be a much-improved quarter for the Amati Strategic Metals Fund, although it was really one of two halves (figure 1). The metals market rebounded strongly in April and May from the very oversold levels that we witnessed in the first two months of the year. The copper market was subject to a speculative price squeeze by investment funds which resulted in copper prices topping US$5/lb in May before pulling back as anticipated strong physical demand from China failed to materialise. The disappointing US and Chinese May manufacturing numbers resulted in softer commodity prices across the board in June.

The precious metals market had been particularly strong from March through to the end of May as the market started to anticipate the first rate cut in the US. However, news that the Chinese central bank stopped buying gold in May and June, after 18 consecutive months of purchases, caused a slight pullback in the gold price. Gold equities sold off significantly in June on the back of this news – a reflection of the continued fragile nature of sentiment towards gold equities.

The battery metals sector also started off the quarter well but was sold off aggressively in June due to market concerns about the growing influence of right-wing parties in the European Parliament following the election results on June 9 and the growing possibility of Donald Trump winning the Presidential elections in the US, both seen to be negative for the sector. The fund was down -3.92%, against the benchmark that was down 1.40%. Since we had 59.9% exposure to precious metals in the fund, mostly in the mid-cap and developers, as well as 17.2% exposure to Lithium stocks, the fund underperformed the benchmark.

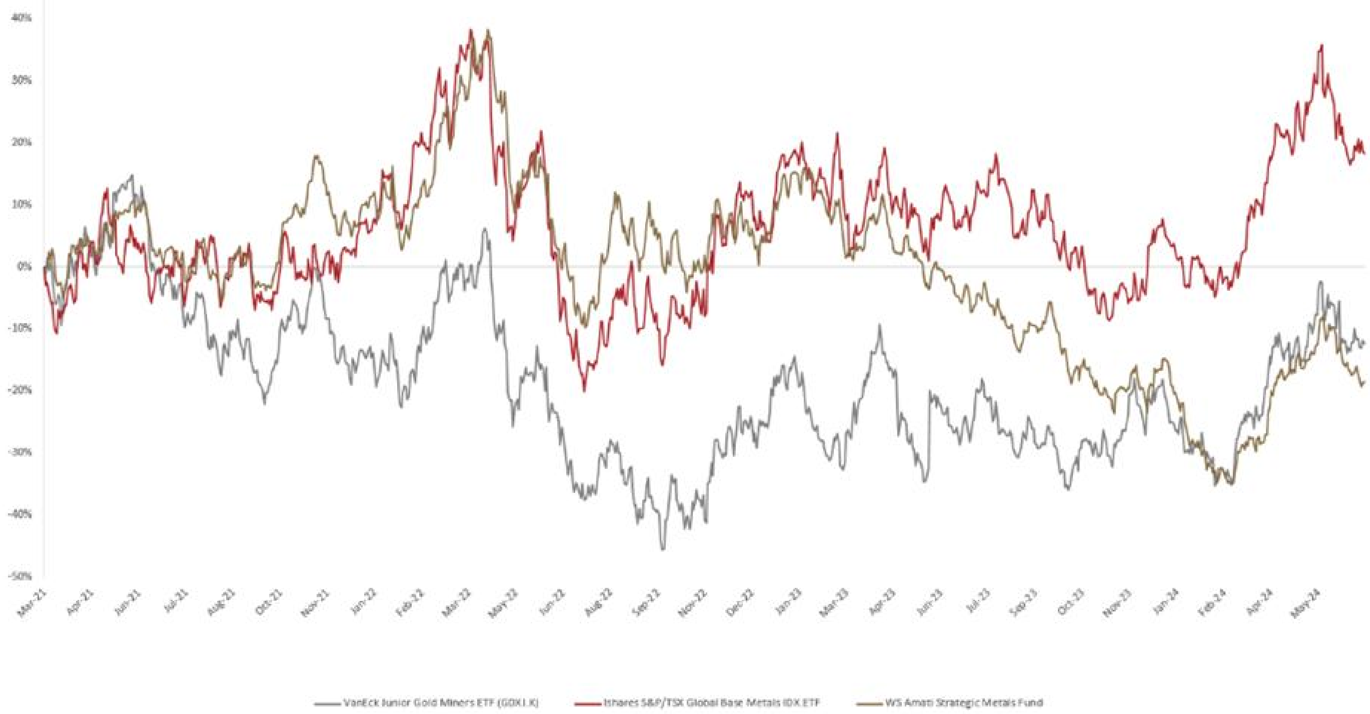
Figure 1: Mining Sector Performance Q2 2024



Performance is calculated in USD. MSCI World Mining current sector weights are: ~47% diversified, ~22% steel, ~19% gold, ~11% copper, ~1% other.

Source: RBC Capital Markets

Figure 2: Fund Performance vs Base Metals & Gold



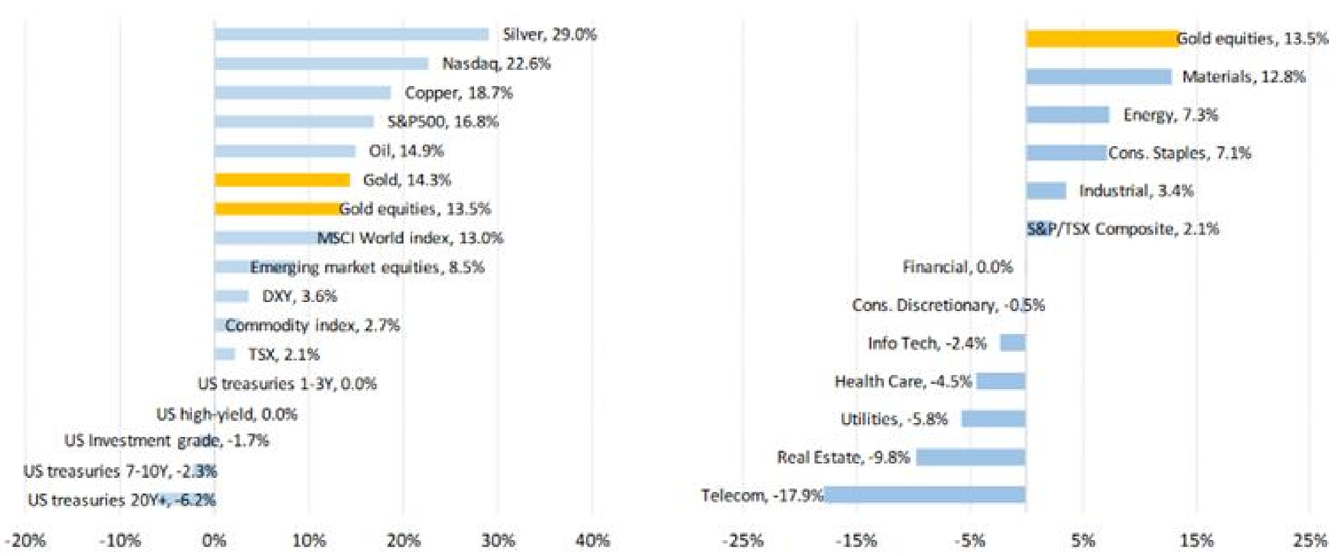
Source: Refinitiv as at 30/06/2024

Precious Metals

Although both the Bank of Canada and the European Central Bank cut interest rates by 25 basis points during the quarter, the US Federal Reserve kept interest rates unchanged but indicated its intentions to cut rates soon, which buoyed the market. The market is now pricing in the first rate cut in September and another before year end. Monetary policy in the US is still dominating sentiment towards the precious metals sector, equities in particular.

Both silver and gold prices have already performed very well since the start of the year (figure 3), with silver even outperforming the Nasdaq Index.

Figure 3: 2024 YTD asset class performance (in USD)



Source: Canaccord Genuity

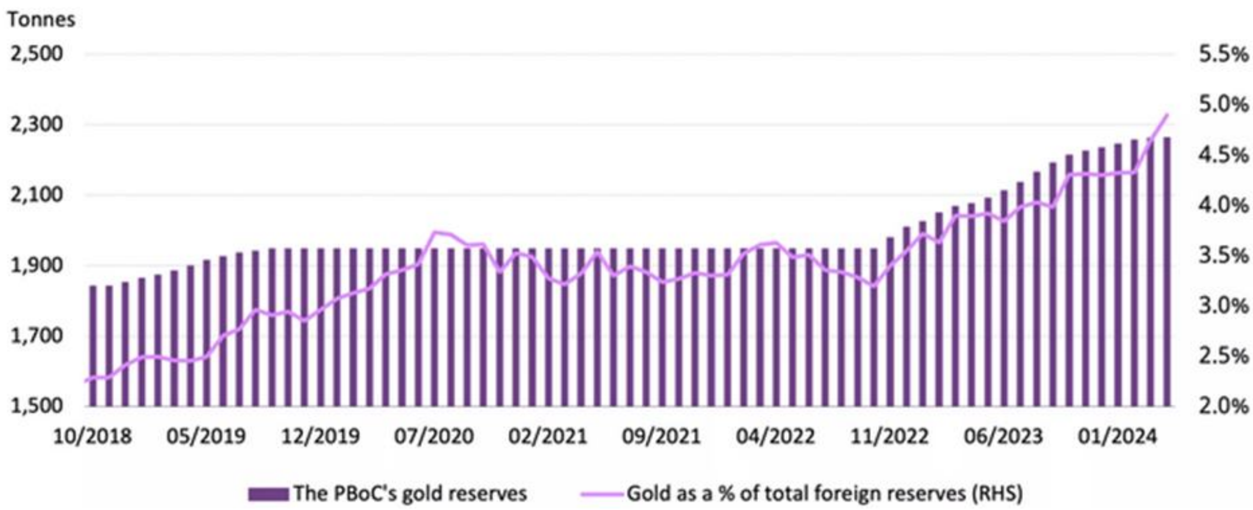
Despite record profit levels, gold and silver equities continue to trade at near record low multiples (Figure 4). On average, the margin between the all-in-sustainable-costs (AISC) and the gold price received for the gold mining industry is now nearing $800/oz. This is an average with many companies reporting net profit margins of over $1,000/oz. We believe that the low valuation metrics are a function of the market's suspicion about the sustainability of the high gold and silver prices that we see on our screens today. Historically, equities usually rally to catch up as gold and silver prices remain elevated for a period of time.

Figure 4: Senior gold producers P/NAV and AISC margins

Source: Canaccord Genuity

Since late 2022, the People's Bank of China have added almost 400 tonnes to its gold reserves (figure 5), partially offsetting 800 tonnes of physically backed gold ETF selling that we have seen in North America and Europe. It is interesting to note that as a percentage of foreign exchange reserves, gold still only makes up less than 5%, highlighting the difficulty that China faces in trying to increase its exposure to gold.

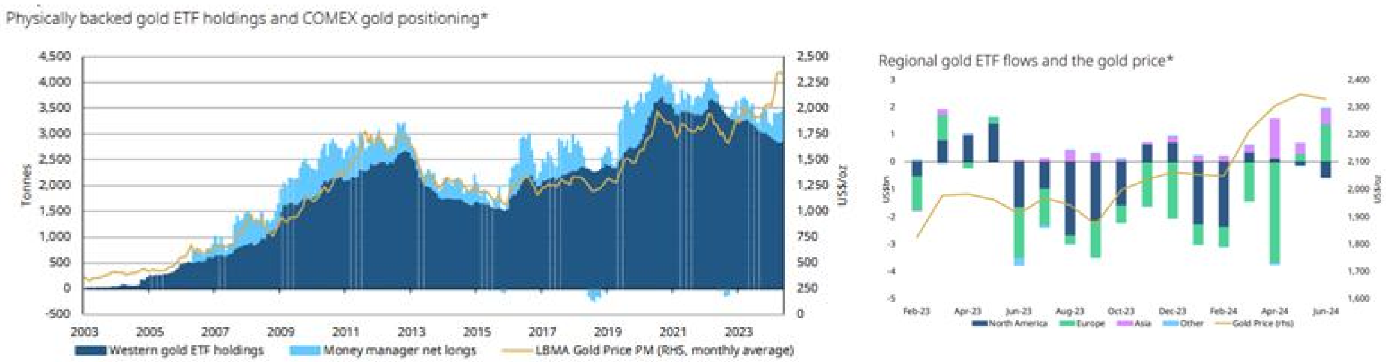
Figure 5: Official Chinese gold reserves (tonnages) and share of total foreign exchange reserves



Source: World Gold Council

China's problem in accumulating gold is expected to prove even more difficult going forward as ETF selling in the West is starting to reverse in anticipation of the start to the rate cut cycle as well as rising geopolitical tensions (figure 6). There is no doubt that the People's Bank of China's purchases have been important for the gold market in recent years during a period where we saw heavy selling of gold in the form of ETFs by investors in the West, its importance has maybe been overstated as the gold price continues to climb higher despite the Chinese stepping back from the market. This is seen as very positive as the first rate cut in the US approaches and ETF buying resumes.

Figure 6: Signs of a return of investment demand for gold in May and June

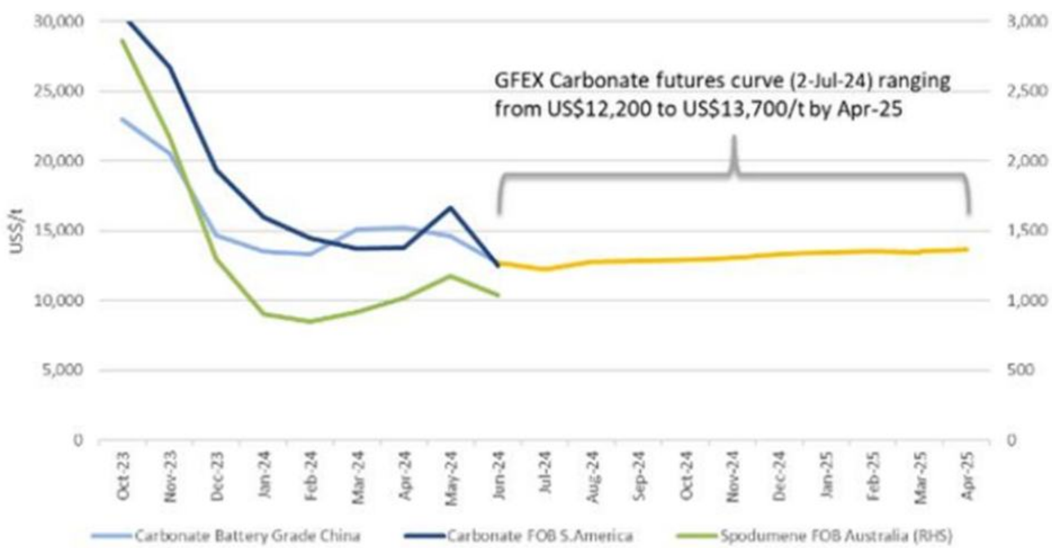


Source: World Gold Council

Critical Metals

The battery metals sector was shaken by the strong showing of right-wing parties in the European Parliamentary elections in early June with the market quickly pricing in the risk of the stringent carbon emissions targets for Europe not being enforced or watered down. Although China is powering ahead with the rollout of electric vehicles, sales in Europe and North America have stalled somewhat after the take-up by early adopters. The growing risk of Donald Trump, a vocal opponent of electric vehicles, returning as President in the US, further soured market sentiment towards the battery metals sector. The reality is that the lithium and nickel price lows that we saw in January and February were clearly not sustainable as half the lithium producers and about a third of the nickel producers were operating at a loss. Prices started to recover in April and May but have since pulled back a bit. Interestingly, the futures curve remains positive suggesting a gradual recovery in pricing over the coming months (figure 4), suggesting support at these levels.

Figure 7: Lithium prices dipped again in June but improvement intact



Source: Petra Capital

Outlook

The mining sector seems to be on the path to a recovery after a difficult first two months of the year. June felt like a pause in the recovery cycle and the sector has already resumed its recovery in early July. Precious metals continue to be our preferred sector for now with high gold and silver prices persisting and looking to move higher, which should lead to very strong financial results for the companies over the course of the year. Rate easing cycles has historically proved very favourable for investors in gold and silver equities and shares are still trading at the most attractive multiples seen for decades.

The battery metals sector is expected to recover over the coming months. Lithium and nickel prices are currently trading at unsustainably low levels, which should lead to future production curtailments and project postponements. The underlying equities look very oversold at the moment and should recover as greater clarity with regards to decarbonisation initiatives becoming apparent in the coming months. We maintained our exposure to lithium at 16% during the quarter.

The portfolio is 32% invested in specialty metals and 60% in precious metals (the 2 book ends to the fund). In lithium, nickel, rutile, and graphite, we hold investments in what we see as the best quality development projects in the world, in safe jurisdictions with projected production costs in the lowest quartile of the cost curve.

The themes that we launched the fund on are still very much intact and we are very reluctant to change the portfolio too much, even more so during times of very low market liquidity.

M&A activity has started to pick up in the precious metals sector in 2024, with **Reunion Gold** subject to a takeover bid by **G Mining Ventures** (both held in the Fund). **Trident Royalties**, another investment in the Fund, was also subject to an all-cash takeover bid by Ecora Resources in the quarter.

We expect M&A activity to pick up further in 2024 with the Fund well positioned to benefit. In the lithium sector, equity prices have fallen to such a low level, relative to what can be justified by spot and longer-term sustainable lithium prices, that there is bound to be a pick-up in M&A activity in the coming months.

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Risk Warning

Past performance is not a reliable guide to future performance. The value of investments and the income from them may go down as well as up and you may not get back the amount originally invested. Tax rates, as well as the treatment of OEICs, could change at any time. The investments associated with this fund are concentrated in natural resources companies, which means that the fund is subject to greater risk and volatility than other funds with investments across a range of industry sectors. The fund invests in companies that have operations in developing markets and which therefore may be subject to higher volatility due to political, economic and currency instability. Shares in some of the underlying companies in the fund may be difficult to sell at a desired time and price. A dilution levy may be applied to the share price when the fund is expanding or contracting. Should you buy or sell in these circumstances it may have an adverse impact on the return from your investment.

This review does not provide you with all the facts you need to make an informed decision about investing in the fund. Before investing you should read the Prospectus, the Key Investor Document (KIID) and Supplementary Information Document (SID). The Prospectus sets out the main risks associated with the fund, the KIID shows you how costs and charges might effect your investment, and the SID details your cancellation rights. If you are in any doubt as to how to proceed you should consult an authorised financial intermediary. Fund documentation can be requested from Waystone or Amati and is available to download from our website.