Amati
Global Investors
Finely crafted investments

WS AMATI STRATEGIC METALS FUND

Quarterly Review

September 2024

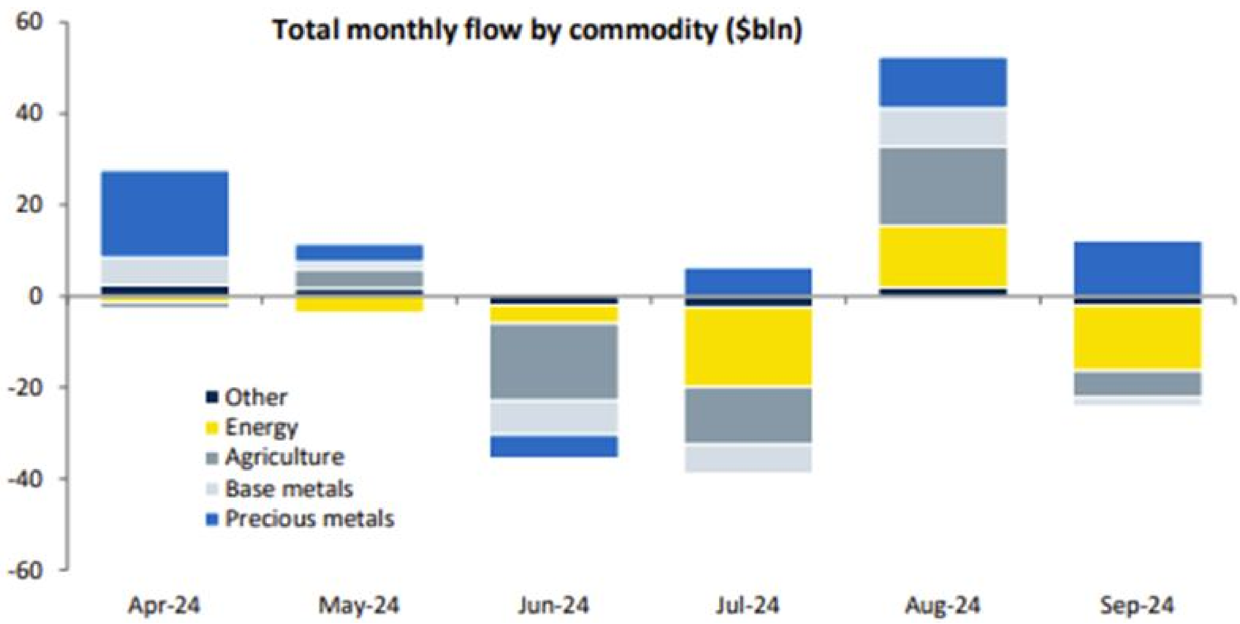
By
Mark Smith, Fund Manager

By Mark Smith, Fund Manager

Gold averaged a new record quarterly price in Q3 of ~US$2,477/oz, +6% vs. the previous record of US$2,336/oz set in Q2 and up 28% vs. Q3/23. For the year, gold has now averaged ~US$2,300/oz, set for a new annual record, 18% higher than last year's record of US$1,943/oz. Silver averaged us$29.46/oz in Q3, its best quarterly average since Q1/13 and up 2.1% q/q and 25% y/y.

The S&P/TSX Gold index (in US$) jumped 18% in Q3, its best performance since Q1/22. This trend was mirrored by investor assets under management, staging 3 positive monthly inflows. The WS ASMF was up 1.5% during Q3.

Figure 1: Total monthly flow by commodity (US$bn)



Source: RBC Capital Markets

The key date in the quarter was 23rd August 2024. US Federal Reserve Chair Jerome Powell said "the time has come" to begin lowering interest rates. A 50bp cut happened. Gold hit an all-time high on the announcement of US$2531/oz. Since September 18th, gold has continued to push higher on continued central bank and ETF buying, and higher geopolitical risk (Middle East/Ukraine).

China reduced the central bank's reserve requirement ratio by 50bp in a bid to support the waning stock and property markets. The Central Bank guided to another 20-50bp cut by year-end. PBoC stated that these measures would add US$142bn in liquidity to the banking system. US$71bn was released to help brokers and insurance companies buy stocks, with US$43bn also being provided to support share buybacks. In a bid to support the property market, Beijing also lowered mortgage downpayments for second homes to 15% from 25%. The Central Bank will also support local governments to buy up unsold inventory from defaulting property developers.

This provided a boost to the base metal, industrial metal and battery metal complexes. However, with the western world slow down in EV sales, the lithium and battery metals market still faces headwinds. Although global EV sales were up 23% y/y in H1/24, there has been a clear pivot to plug-in hybrids (PHEV). Chinese sales were up 38% YTD y/y in H1/24, however auto OEMs in western markets have delayed electrification targets and reduced EV plans and investment. The mining industry has responded with nearly 400kt of mining capacity coming offline. The decline in lithium commodity pricing has pushed the industry to (1) review and rationalize operations; (2) implement significant cost cutting measures to preserve cash flow; (3) curtail production; (3) delay expansion projects; and (4) defer investments into new capacity.

Company responses:

- **Operational Reviews:** Core, Pilbara, Albemarle, Arcadium, Piedmont, Sayona, and Sigma.
- **Cost-Cutting Measures and Cash Flow Preservation:** Albemarle, Pilbara, Core, and Sigma.

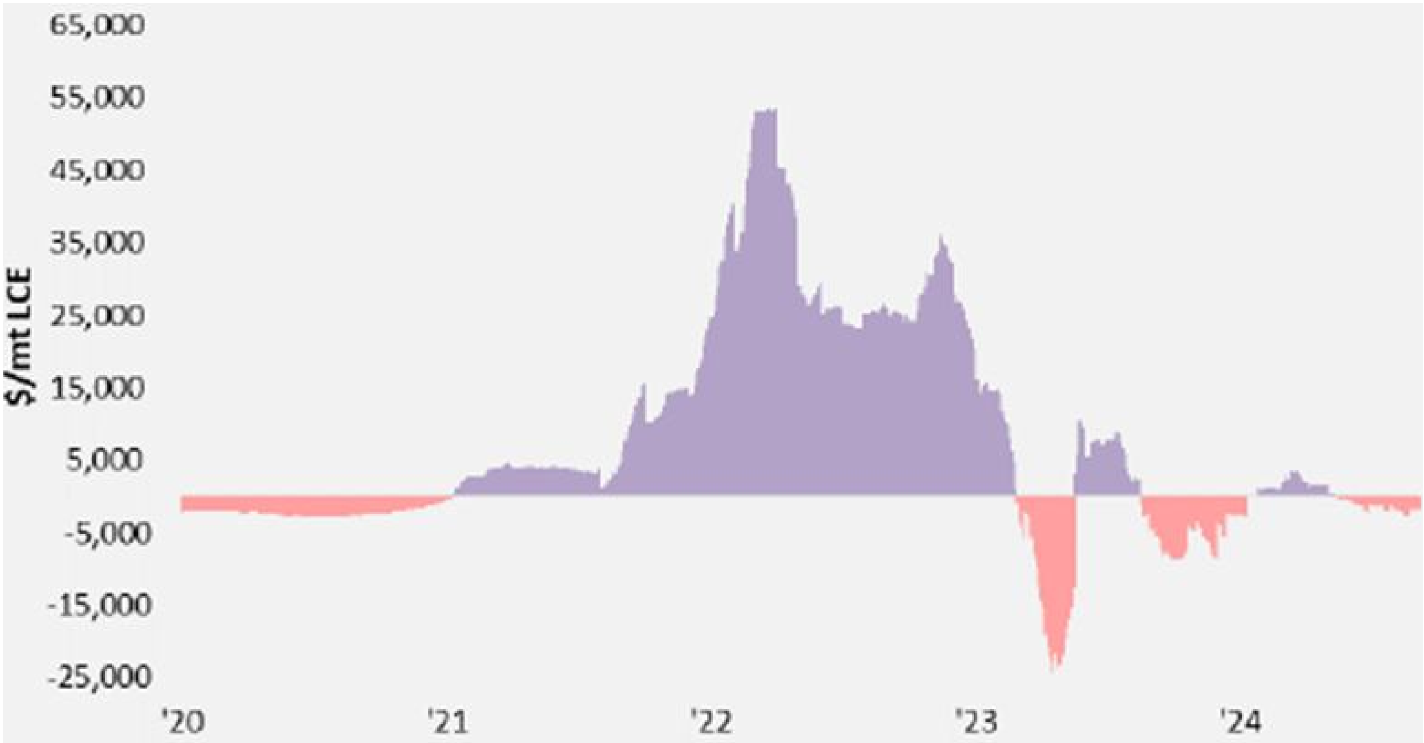
By Mark Smith, Fund Manager

- **Supply Cuts: CATL, Tianqi, Core, IGO, MinRes, and Albemarle.**
- **Project Delays and Deferrals: Albemarle, Arcadium, Liontown, Core, Ganfeng, Rio Tinto.**

For investors, the debate has narrowed on marginal cost. Most believe the current price is unsustainable if various levels of government in China stop financially supporting unprofitable (non-integrated) operations. We believe lithium prices could rise and might not continue to be supply (cost curve) driven because of the positive effects of (1) downstream channel restocking/destocking; (2) EV supply-chain seasonality; (3) delays/deferrals to new capacity pushing back LCE availability; and (4) demand surprising to the upside on government incentive schemes and the falling price of the battery units.

We monitor the profitability of the lithium conversion capacity, which currently remains unprofitable, on average. The average refinery/converter may not be breaking even. This situation doesn't last long, with a jump up in lithium carbonate pricing. We can trade around this market and theme.

Figure 2: Lithium carbonate refining margin development



Source: Scotia Bank

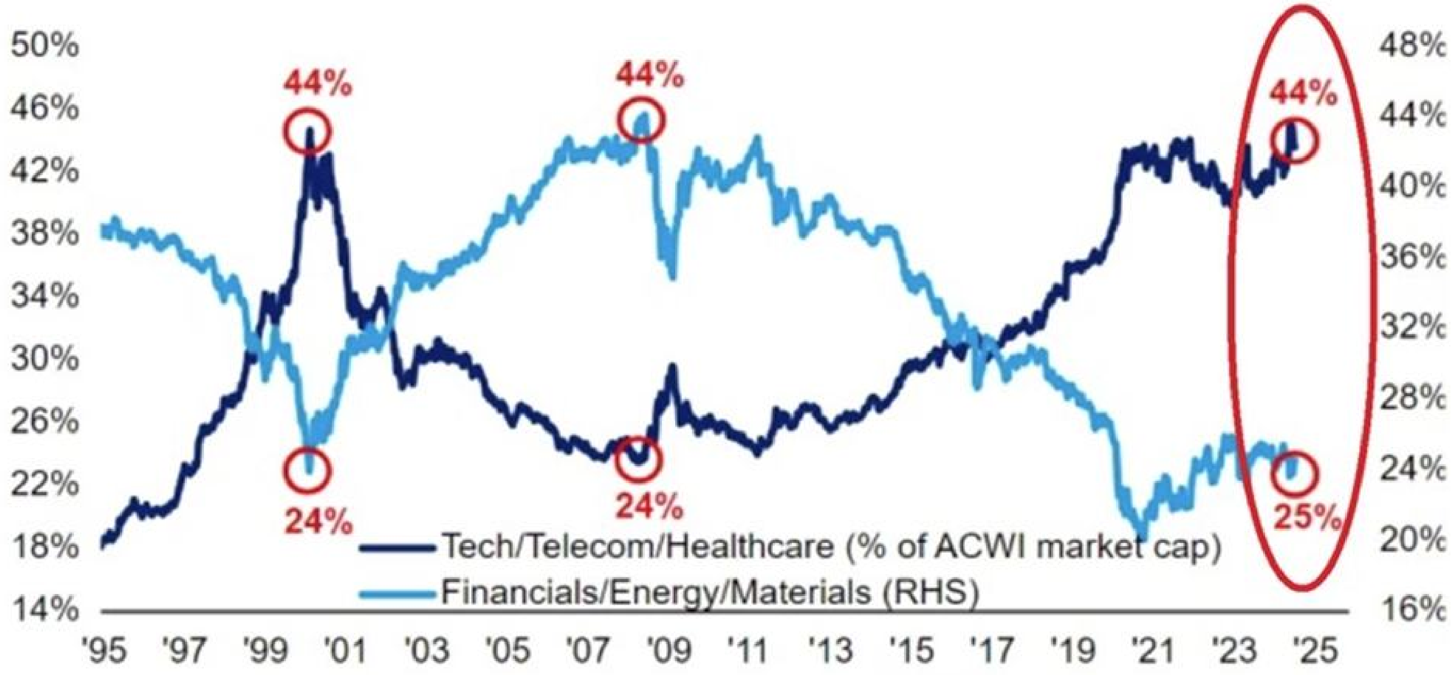
Generalist investor interest still on the sidelines

The mining industry will require US$2.1 trillion in new investments by 2050 to meet raw material demands of a net-zero emissions world (according to BloombergNEF). This capital will have to be supported by broader money supply, not just the resource investor and government loans.

The crowded TECH trade – The market concentration for Tech/telecoms and healthcare has peaked at 45% share of the global equities. This concentration has reached the levels of the dot-com bubble of 2000. The downtrend in investor appetite for metal equities is highlighted by the GSCI Commodity Index vs the S&P 500 ratio which sits at a 50 year low. Interestingly, when you plot the GDX, GDXJ, Industrials sector (XLI) and Technology sector (XLK) against a benchmark of the S&P500, it shows large institutional money profit taking in tech/growth, with rotation into value, and commodities setting up to catch up. We expect (hope) the generalist investor will follow suit, setting up a broader, sustained rally in metal/mining equity markets.

By Mark Smith, Fund Manager

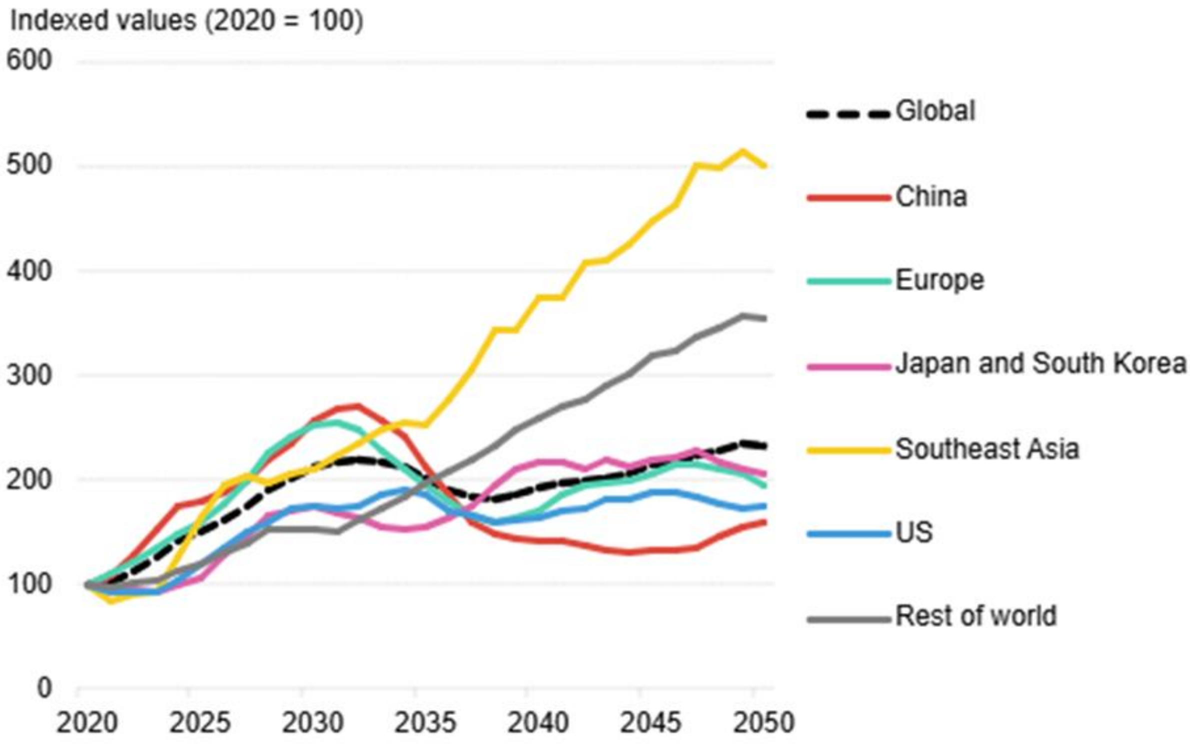
Figure 3 – Sector market concentration of Global Equities



Source: BofA Global Investment Strategy

According to BNEF's Economic Transition Scenario (ETS), which assumes no new policy support and is driven by the cost competitiveness of technologies, the world may need 3 billion tonnes of metals between 2024 and 2050 to support low-carbon solutions such as electric vehicles, wind turbines, and electrolyzers. That figure could rise to 6 billion tonnes to achieve net-zero emissions by 2050. Of the 11 energy transition metals with mined supply tracked in this study, eight are exposed to significant supply chain risk.

Figure 4: Growth of energy transition metals demand relative to 2020 levels



Source: BloombergNEF

By Mark Smith, Fund Manager

Outlook

The trilogy theme continues: US FED rate cuts, Chinese Central Bank stimulus and heightened geopolitical risk. The first two are macro-scale bullish price drivers for precious metals and the broader metals market. The third undermines investor confidence, reduces capital flow and adds risk to global trade.

With a sustained decline in US rates through to 2026, it will provide further price support for gold and gold equities. There is a possibility that China's Central government expands the scale and duration of its monetary stimulus into 2025 to achieve 5% GDP growth. This will act as a broad-based commodity demand/price driver (steel/inputs; industrial metals, battery metals). The US infrastructure rebuild, once the fully - approved will be a US$1.2tn infrastructure re-build program, again supportive of broad based commodity imports. The negative will be the geo-political tension created by Russia's war; Israel vs the Middel East; China-Taiwan and escalating US trade tariffs should Trump win the US election.

Under all 3 scenarios, the WS ASMF can benefit through the 68% precious metals – 32% battery/base metals equity exposure. The fund's commodity exposure has largely remained the same during Q3. We are overweight gold and silver versus the benchmark, with a c.80% bias to small and mid-cap companies. Interestingly, a new report from Ernst & Young stated capital is the top risk facing the mining industry. About US$1tr is needed to invest in metal production for the energy transition. If the mining companies can't attract investment to grow production, they will look to equity based M&A. We are starting to see M&A in our universe and the fund is positioned by design to benefit from M&A.

Sales Team Contacts

Rachel Le Derf
Head of Sales & Marketing
rachel.lederf@amatiglobal.com
07979601223

Colin Thomson
Head of Intermediary Distribution
Northern England, Scotland & NI
colin.thomson@amatiglobal.com
07884026517

Jonathan Woolley
Sales Director
London, Midlands, SW England & Wales
jonathan.woolley@amatiglobal.com
07818203013

Samantha Dalby
Sales Manager
samantha.dalby@amatiglobal.com
+44 (0) 131 503 9116

Olivia Pattison
Senior Sales Support Executive
olivia.pattison@amatiglobal.com
+44 (0) 131 503 9126

Risk Warning