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Schroder ISF[1] Global Gold Fund update

January 2023

Fund performance:

The fund posted a return of 10.26% for January. This compared to the FTSE Gold Mines Index benchmark return of 11.75%.

I shares gross

US$ %	Jan 2023	Since Inception[1]	
		Cumulative performance	Annualised performance
Fund	**10.26**	**29.00**	**3.94**
Benchmark[2]	11.75	18.62	2.62

Calendar year performance

US$ %	2013	2014	2015	2016[1]	2017	2018	2019	2020	2021	2022
Fund	-	-	-	-	**11.3**	**-13.9**	**51.1**	**31.5**	**-17.1**	**-10.5**
Benchmark[2]	-	-	-	-	10.2	-10.4	42.7	25.0	-10.4	-12.8

Past performance is not a reliable indicator of future results, prices of shares and the income from them may fall as well as rise and investors may not get the amount originally invested.
Source for performance: Bloomberg I shares gross USD. Performance is on a NAV to NAV basis. [1]Inception 29 June 2016. [2]FTSE Gold Mines Index. Typical ongoing charges for I shares are 1.07%.

Risk Considerations:

Capital risk / distribution policy: As the fund intends to pay dividends regardless of its performance, a dividend may represent a return of part of the amount you invested. **Counterparty risk:** The fund may have contractual agreements with counterparties. If a counterparty is unable to fulfil their obligations, the sum that they owe to the fund may be lost in part or in whole. **Currency risk:** The fund may lose value as a result of movements in foreign exchange rates. **Derivatives risk:** Derivatives may be used to manage the portfolio efficiently. A derivative may not perform as expected, may create losses greater than the cost of the derivative and may result in losses to the fund. **Emerging markets & frontier risk:** Emerging markets, and especially frontier markets, generally carry greater political, legal, counterparty, operational and liquidity risk than developed markets. **Higher volatility risk:** The price of this fund may be volatile as it may take higher risks in search of higher rewards. **IBOR risk:** The transition of the financial markets away from the use of interbank offered rates (IBORs) to alternative reference rates may impact the valuation of certain holdings and disrupt liquidity in certain instruments. This may impact the investment performance of the fund. **Liquidity risk:** In difficult market conditions, the fund may not be able to sell a security for full value or at all. This could affect performance and could cause the fund to defer or suspend redemptions of its shares. **Market risk:** The value of investments can go up and down and an investor may not get back the amount initially invested. **Operational risk:** Operational processes, including those related to the safekeeping of assets, may fail. This may result in losses to the fund. **Performance risk:** Investment objectives express an intended result but there is no guarantee that such a result will be achieved. Depending on market conditions and the macro economic environment, investment objectives may become more difficult to achieve.

Current strategy and portfolio activity:

Overall fund strategy remains focused on producers with unjustifiably cheap valuations, clear paths to free cash inflections and/or other value surfacing optionality. These opportunities are clearest in the mid-tier and junior end of the market cap spectrum, though valuation opportunities also exist among senior producers.

The hedge positions which featured in various parts of 2022 are currently significantly reduced within the portfolio. We have one royalty position (royalty companies should also be seen as defensive) within the portfolio. We have zero gold bullion exposure.

The largest shift in fund positioning since the start of the year was a further increase in Pan American Silver funded from a decreased position in Agnico Eagle. After a poor 2022 Pan American has multiple material catalysts ahead of it, a strong management team and is pretty much the only genuine investable "quality" silver producer of any meaningful size which means valuation premiums could well expand significantly.

Gold and gold equity market outlook:

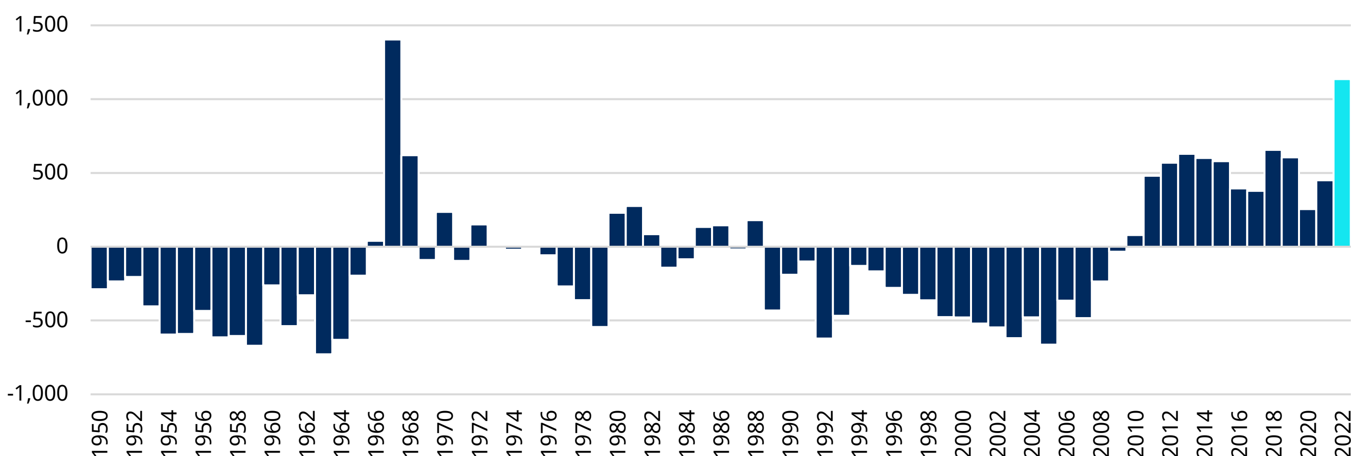
Gold prices sit roughly 7% from the all time high at the time of writing, having just breached US$1,950/Oz.

Given that investors, on aggregate, continue to liquidate ETF ounces and futures positioning remains thoroughly un-stretched, it begs the question of where prices might go if investors do decide to join what has already been substantial buying elsewhere. Meaningfully higher seems probable.

By far the most striking of this buying has been from Central Banks. Fourth quarter 2022 Central Bank purchases again broke records.

We thought we had been overly generous to annualise the first three quarters of 2022 buying in a recent chart, as it turned out we were too conservative. Central Bank demand of 1,136t for the full year was a huge increase on recent year averages and the highest single year since 1967 (see chart 1).

Chart 1: Central Bank purchases of 1,136t in 2022 was the highest full year total since 1967



Source: WGC, Schroders.

Three quarters of these purchases were unreported (as estimated by Metals Focus a London based research firm), much higher than the normal 5-15%. As such there is a lot of opacity as to precisely where these tonnes are going. A good guess would likely involve large economies worried about being on the wrong side of future conflicts with the US, China being the most obvious. That Chinese gold prices have remained at premiums to western contracts even as prices have moved smartly higher is also striking. Are the reported 30t increases in PBOC gold reserves the whole amount? We will probably never know. Alongside usual suspects such as Turkey, reserve additions from Singapore, Ireland, and most recently Croatia are symptomatic of demand that has even broadened into select developed markets.

In 2023 we expect overall "monetary" gold demand, the totality of bar and coin, central bank and physical ETF demand, to remain very strong. Can Central Bank demand be replicated at 2022 levels? Who knows, though it is worth reflecting that while 1,100 tonnes (c.US$65bn at average 2022 prices) represents a sizeable 24% of 2022 gold demand it is a drop in the ocean of current global monetary excesses. US$65bn is roughly 30% of what Japan spent defending bond yields in January 2023 alone, is less than a single month of China's recent trade surpluses ($80bn in December), and only equivalent to around 2% of total China FX reserves.

Overall, the environment for continued "monetary" accumulation of gold remains resoundingly positive even if forecasting precisely how that will be divided between Central Banks, super high net worth individual, sovereign wealth funds and involutional investors is very tricky.

Whether the US falls into recession and how Jerome Powell and his committee respond is far from the only cyclical driver of gold markets, but it is clearly important judged by the number of questions we have had on it. Historically gold has done well

through US recessions and gold equities have done even better. That is summarised in the table below taken from a report we recently wrote on this topic.

Exhibit 1: Gold and gold equities performance through historic US recessions

Recession Year	Recession Length (months)	Gold bullion performance (absolute) %	Gold bullion vs. S&P performance (relative) %	Gold Stocks[1] performance (absolute) %	Gold stocks[1] vs. S&P performance (relative) %
1973	16	39	79	85	131
1980	6	71	37	184	125
1981	16	-14	-31	8	-10
1990	8	-14	-27	-22	-35
2001	8	19	60	103	174
2008	18	69	128	39	88
2020	2	24	11	28	14
Average	**11**	**28%**	**37%**	**61%**	**69%**

Source: Schroders, Bloomberg, Barron's Gold Mining Index, NBER. Notes: [1]Gold stocks performance represented by Barron's Gold Mining Index (BGMI) for 1973, 1980, 1981 and 1990 recessions and the FTSE Gold Mines Index for 2001, 2008 and 2020 recessions. Recessions defined using NBER US Recession Indicator.

The exceptions to this strong performance were 1981 and 1990. 1981 was the Volcker shock whilst 1990 was a mild recession in a gold market characterised by the start of a flood of Central Bank sales. As such we see neither example as likely to be repeated today. Given the US is approaching a potential recession with very high deficits, very high debt, as well as a dysfunctional domestic political situation (as well as a looming debt ceiling) we think the policy response to any US recession will need to be highly accommodative and involve a return to combined fiscal/monetary support. This is because extremely high aggregate debt levels and large deficits mean the chance of a normal cyclical recession morphing into something much worse will remain far too high for policymakers to risk, whether that is explicitly admitted or not. Therefore, we just don't believe Jerome Powell's attempts to invoke Paul Volcker have any chance of success beyond the very short term. For the full report see here.

For the gold equities, as we move through full year 2022 results, we are overall becoming more comfortable with the notion that cost expectations have been broadly reset and companies will have a much easier time staying within guidance ranges in 2023 than they did in 2022. We will update a fuller view of 2023 cost guidance's next month once all the producers have guided.

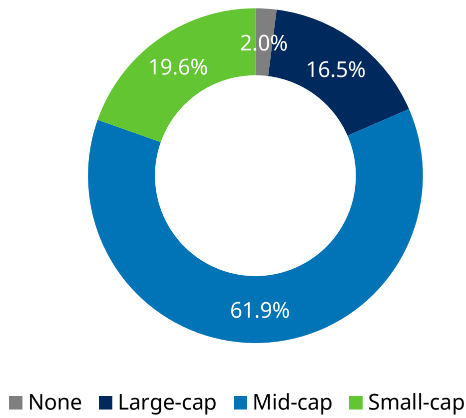
We also think that the Agnico/Pan American combined offer for Yamana (trumping Goldfields) could finally trigger a rush of further consolidation, with combined bids for companies likely to feature in that. This view has been reinforced by the significant news in the sector, coming after month end, of Newmont's ~$16.9bn indicative offer for Newcrest, representing a 21% premium to Newcrest's pre-announcement close price. This deal would see Newmont become the largest gold producer globally with the combined entity having a market cap of ~$54bn and producing ~8Moz of gold. We expect this industry consolidation theme to continue and move into the mid-tier and junior producers space as, in our view, there are several very logical combinations possible.

Despite strong gold price momentum the more defensive royalty producers have again outperformed the broader sector YTD. This should hammer home the message to producers that resilience (financial and jurisdictional), in an increasingly volatile world, will be key to regaining valuation traction and any interest with generalist investors.

Performance attribution:

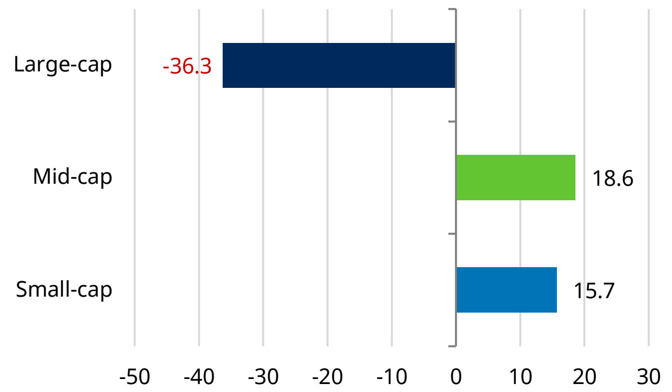
Fund performance in January was 11.07% compared to 11.75% for the benchmark. Negative attribution from structural underweight positions in Barrick and Newmont was partly offset by positive attribution from overweight positions in Resolute and Westgold, who outperformed following better than expected quarterly results, as well as from our larger overweight positions in Eldorado and Pan American.

Market cap (%)



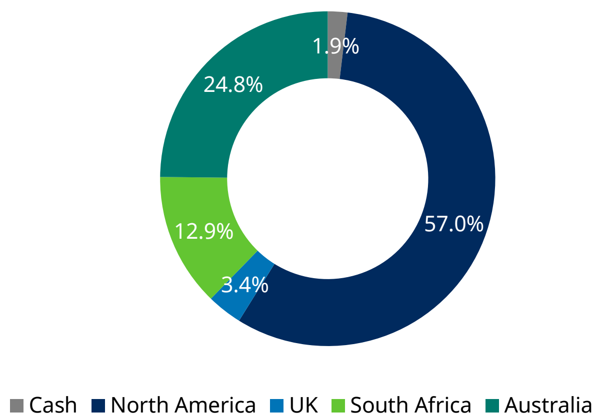
Source: Schroders, Bloomberg – January 2023.

Market cap over/underweight (%)



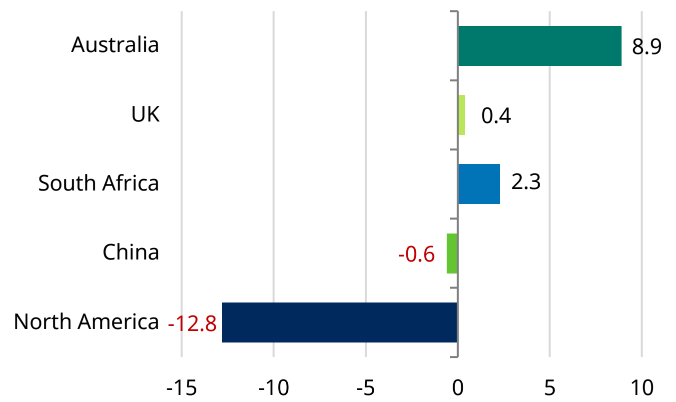
Source: Schroders, Bloomberg – January 2023.

Regional (%)



Source: Schroders, Bloomberg – January 2023.

Regional over/underweight (%)



Source: Schroders, Bloomberg – January 2023.

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