Ninepoint Gold & Precious Minerals Fund

September 2019 Commentary

As the trade war continued to fuel volatility across global equity exchanges, the Ninepoint Gold and Precious Minerals Fund continued its strong performance in 2019. At the end of Q3, the strategy was up 13.03% YTD and returned 6.94% over the course of Q3 2019.

While Q3 was positive overall, the month of September saw gold and gold equities take a necessary breather after a torrid July. We had anticipated this and prepared for this by increasing cash levels and reducing exposure to higher volatility names. Our proactive focus towards risk mitigation and volatility reduction has translated into significantly lowered volatility and beta versus the indices.

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The top three contributors to the fund performance in the third quarter were Dacian Gold, Ramelius Resources and Echo Resources. Dacian recently brought its West Australian Mount Morgans Gold operation into production and encountered operational difficulties, cutting short- and medium-term production outlook. The stock consequently lost almost 80% of its value from January to June. The market over penalized the stock in our view. In Q3 the company made strides towards regaining investor confidence as it provided an updated 8-year mine plan in July and an in-line June quarter. Dacian appreciated 160% in Q3 becoming the top contributor. Ramelius is also a West Australian producer and has been delivering consistent production and financial results. The company announced a 5 year mine plan giving visibility into its production profile. The stock appreciated 55% in the quarter, but remains one of the cheapest names in our universe as measured by enterprise value to production ounces. Echo is an Australian gold explorer with the key asset being the Bronzewing Processing Hub, which is a strategic asset in the area. On August 26th, the company announced that it had entered into a Bid Implementation Agreement, pursuant to which Northern Star Resources would offer to acquire all of the issued and outstanding ordinary shares in Echo at $0.33 per share in cash. The offer represented a 32% premium to the last closing price of Echo.

The top three detractors from the fund performance in the third quarter were Energold Drilling, Semafo and White Gold. Energold.... Semafo is a West African explorer operating two gold mines in Burkina Faso. The stock was an outperformer in the second quarter, but came under pressure in Q3 because the company announced in early August that a pit wall had failed at one of its mines – this has pushed about 45,000 ounces of 2019's production into Q1 2020. As such, the company reduced its 2019 production guidance. We feel this name represents very good value given its free cash flow generation profile. White Gold is exploring its extensive property package in the Yukon including its flagship Golden Saddle & Arc deposits. The company has announced multiple encouraging drill results from the summer exploration program, including a new high grade gold

discovery and has identified multiple additional high-priority targets.

While silver has continued to trade at frustratingly low levels, we look towards gold to set direction for the price of silver. Gold bullion traded at a six year high in September 2019, making a new high of $1552/oz. Despite gold trading almost 14% higher than the 2016 peak of $1366/oz, the GDX failed in its attempt to surpass the 2016 high. The GDXJ was even worse off, trading almost 20% below its 2016 high.

The combination of rising bullion prices and investor apathy towards precious metals equities has created a potent mixture for precious metals investors. As bullion prices continued their march higher during the third quarter, we saw something entirely unexpected occur in the precious metal equity funds and related ETFs. Outflows.

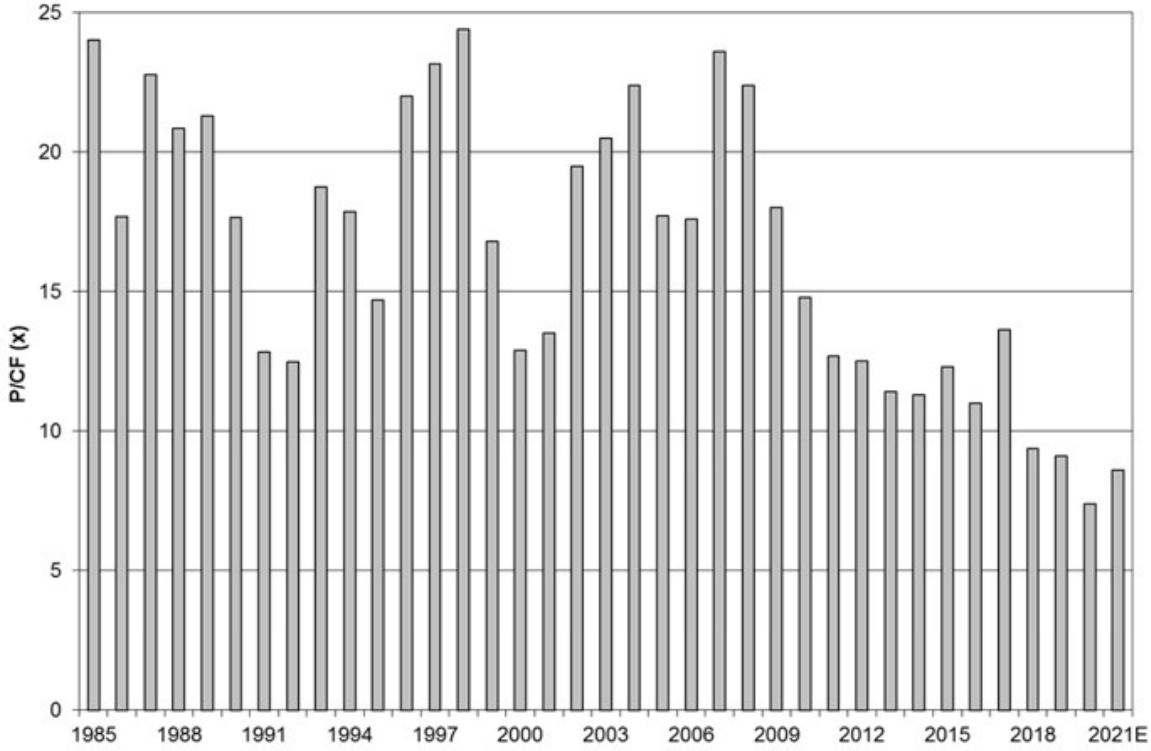
Source: Bloomberg

The chart above graphs the year-to-date shares outstanding in the GDX and GDXJ ETFs. As precious metal equities experienced strong gains in June and July, investors responded by redeeming their units for cash. Over the course of the first three quarters of 2019, investors have redeemed 82.10M shares of GDX and 27.70m shares of the GDXJ. This represents 16.36% and 19.52% of shares outstanding for the GDX and GDXJ respectively – a truly staggering amount.

This behavior was not confined to passive vehicles such as ETFs because we saw the same pattern emerge from investors in actively managed precious metal equity funds as well. These divergences are unusual and uncommon, especially given two very important factors.

1. The precious metals sector today are far more leaner and profitable than they were the last time we saw gold prices around $1500/oz after having endured a six year bear market in bullion prices. Senior precious metal equities today trade at one of the lowest P/CF multiple in over thirty years.

Senior Producer Price to Cash Flow Multiples



Source: Scotiabank

2. Similarly, precious metal equities have never been as cheap in over thirty years when measured against their Net Asset Value (NAV). The chart below, courtesy of Scotiabank graphically demonstrates this point.

Source: Scotiabank

The chart below is a classic and it captures investor sentiment at various phases of the market cycle.

We surmise we are currently somewhere between the two Ds of the market cycle, namely, between despondency and disbelief. Following the classic capitulation we witnessed at the end of 2015, investors have been downright despondent and doleful towards precious metals investing over the past few years despite strong returns. The GDX and GDXJ have returned 97.80% and 99.75% from Jan 2015 through September 2019 inclusive of dividends far outperforming the S&P 500 which returned 57.20% including dividends. Equity investors have met the 2019 rally in bullion prices with disbelief. They have responded by cashing in their gains in gold and silver equities, afraid that they may never see these prices any time soon. Therein lies the opportunity for savvy investors who recognize the bargain represented by silver equities.

NINEPOINT GOLD & PRECIOUS MINERALS FUND - COMPOUNDED RETURNS[1]

	1M	YTD	3M	6M	1YR	3YR	5YR	10YR	INCEPTION
Fund	-11.0%	13.9%	7.2%	10.8%	27.8%	-6.2%	6.5%	-0.5%	1.7%
Index	-10.4%	27.1%	7.0%	21.1%	54.0%	0.7%	8.2%	-2.5%	1.6%

[1] All returns and fund details are a) based on Series F units; b) net of fees; c) annualized if period is greater than one year; d) as at September 30, 2019; e) 2001 annual returns are from 11/15/01 to 12/31/01. The index is 100% S&P/TSX Global Gold Total Return Index and is computed by Ninepoint Partners LP based on publicly available index information.

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