MANAGER UPDATE

Henderson Horizon Global Natural Resources Fund

September 2014 **For professional investors only.**

The value of an investment and the income from it can fall as well as rise and you may not get back the amount originally invested

Natural resource opportunities – based on an award winning approach

Just over two months after the launch of the Henderson Horizon Global Natural Resources Fund, lead manager, David Whitten outlines his investment approach and the opportunities currently being uncovered.

"For natural resource investment, quality is paramount"

We believe in the genuine active management of high quality assets based on rigorous bottom-up analysis. The substantial expertise of the investment team, comprising a geology, mining and agriculture specialist, allows us to target quality companies with competitive advantages, robust business plans and excellent management. The fund provides a high conviction portfolio of quality natural resource stocks sensibly diversified by commodity, geography, size, maturity and investment strategy. These we blend with a tactical tail of risk-adjusted, high growth, smaller stocks. The universe we invest in includes energy, mining, and unlike many competitors, agricultural companies, offering a broad range of opportunities.

"A truly exciting, under-researched, potentially world-class mineral discovery that has never seen a buy or sell investment recommendation? These are the opportunities the team relishes – the ethos is 'What are we waiting for, jump on a plane and visit the project!'"

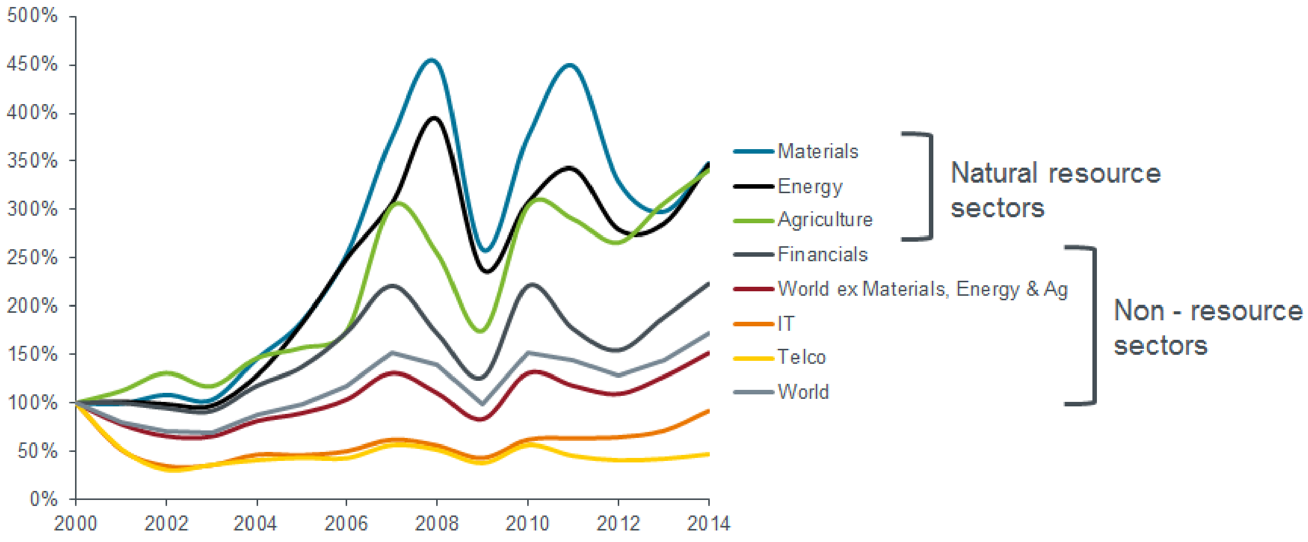
We are agnostic in terms of investment style with stock selection utilising both growth and value screens. A robust risk framework is maintained and we ensure that high conviction investment ideas have a meaningful impact on overall portfolio returns. An emphasis is placed on hands-on, independent analysis and research when required, and more opportunities tend to be found within the less well covered supply-side analysis rather than the well-researched demand side. Far from being put off by a lack of coverage, we are keen to, and well capable of, forming our own expert view, and this has historically helped drive returns.

Current opportunities

The breadth and depth of the fund's natural resource universe means we are always able to find opportunities up and down the supply chain. Our approach is currently generating particularly compelling and interesting investment ideas.

The sector as a whole has a number of drivers lending support. Key among these are: population growth in less developed countries; urbanisation; and productivity, in the form of rising gross domestic product (GDP) and industrial production (IP) per capita. The combinations of these drivers have led to an increase of the importance of natural resources relative to other global equities. In 2000 natural resources accounted for 13.3% of the global total; in 2014 they made up 24.7% with strong market capitalisation growth across materials, energy and agriculture (see chart overleaf)

Market capitalisation - % growth 2000 – 2014



Source: Bloomberg, as at June 2014. 90 West analysis based on world's 3,000 largest stocks split by GICS sectors for mining & energy from 2000 to 2014. Agriculture is 90 West defined guided by S&P GICS agriculture sub-industries.

Within the three major sub-sectors, there are specific opportunities:

Energy

Certain oil and gas production companies in North America are benefiting from the **rapid technological improvements** in the process of horizontal drilling, hydraulic fracturing (known as 'fracking') and extraction of oil from shale and associated rocks.

Those 'upstream' operations with prime assets, first mover advantage and large resource positions offer particularly attractive investment opportunities. Down the pipeline, or 'mid-stream', we maintain exposure to US companies involved in **energy transportation**. This allows us to take advantage of the rapid volume growth and the fact high quality companies in this area exhibit strong and predictable growth, high returns on capital and generally operate with relatively low exposures to commodity price risk.

The Interstate Natural Gas Association of America estimates that US companies need to build more than US$600bn worth of **pipeline, storage, and related equipment** during the next 20 years. We have several investments in this area that are well placed to benefit, with competitive costs of capital and difficult-to-replicate energy infrastructure footprints. Consolidation of this sector is also anticipated to accelerate.

The US is set to become a significant exporter of liquefied natural gas (LNG) from 2015. Several companies enjoy highly competitive low natural gas input costs, combined with location and transportation advantages, particularly in the Gulf coast region of Louisiana and Texas.

Mining

Large cap diversified miners are likely to benefit from ongoing cost cutting, capital restraint and a renewed focus on capital management. After three years of downgrades, evidence is mounting that the overall free cash flow cycle is recovering, especially in the under-performing bulk minerals mining sector. Once debt is paid down further, it is likely that the sector will return to substantial free cash flow generation resulting in increasing returns to shareholders via increased dividends and potential share buybacks. Share price valuations are in some cases at multi-year lows.

Typically at this stage of the metals and mining investment cycle, opportunities present themselves for **smaller, more nimble companies.** Those with strong management teams can selectively acquire good mining projects that are seen as non-core by majors. With their lower cost structures and operational focus, these mines can prosper under new corporate structures. De-mergers of non-core assets, particularly within the base metals sector, also provide opportunities.

Gold sector consolidation. Our process concentrates on identifying companies with large high quality reserves, low operating costs, brown fields expansion potential and strong exploration upside. These are the projects that are also the most likely to be acquisition targets by the gold majors.

We see some major mine closures, based on natural depletion, over the next few years affecting the **supply/demand balance** for some commodities such as zinc and nickel and copper. We have invested in several companies bringing on new low cost supply at what we believe is an opportune time. The time and expense to discover, permit and bring on major new mines has increased to such an extent that any dislocations in the supply/demand balance can take a long time to rectify. We therefore expect companies with outstanding natural reserve advantages to prosper.

Agriculture

The growth outlook for some large traditional northern hemisphere agricultural companies is being turbo-charged by agricultural growth opportunities in the southern hemisphere, especially in places such as Brazil. Apart from the advantage of complementary planting, growing and harvesting seasons between hemispheres, many of these new agricultural areas offer abundant arable land and a transportation advantage to strong population growth regions. It is large global businesses with a strong global reach for industry leading products and services, which we believe, will continue to thrive.

Growth in **'precision farming'** and the use of data and technological breakthroughs assist growers to increase yield and better manage their crops is a strong driver. Several companies are leaders in developing these technologies and it is likely that a first mover advantage will bring disproportionate investment gains.

Changing global diets, especially the increasing demand for protein, will be present for years to come. Many of the companies we invest in will benefit from the ongoing volume growth and need to continuously increase crop yields directly related to protein demand, such as animal feed crops including soy bean and corn. Accelerating demand for healthier eating in many western countries is creating opportunities for fast moving innovative companies on the cutting edge of this trend.

Assessing and balancing the risks

Natural resource commodity prices and market sentiment remain closely linked to GDP growth, industrial production and global demand. To reduce the macro risks of shifts in fortune and to capitalise on the fact that individual commodities have differing supply/demand drivers, it is important to maintain a well-diversified portfolio spread across sub sectors and the supply chain, and implement a risk overlay that errs on the side of caution.

Volatility tends to be higher in natural resources stocks than other global equity sectors, with investor sentiment swinging across the cycle. Many new natural resource projects are increasingly located in countries and jurisdictions of higher political, environmental and social risk and geopolitical events can have unpredictable impacts. Maintaining a diversified portfolio and ensuring risks are closely monitored are therefore essential to reducing the fund's overall volatility and delivering more consistent investment returns.

It is also important to understand that many natural resources projects, particularly those 'upstream', have long lead times and require large amounts of capital. Therefore the wider market may be unable to accurately value companies associated with these projects until late in the process. Significant experience is therefore required for informed investing; it does also mean that a competitive advantage is available for those with this expertise and also longer investment time horizons.

For the reasons above we do not speculate on the short term outlook for commodity prices.

> *"If you ask me 'What's the gold price going to do?' I will tell you: 'It is going to go up, then down – but not necessarily in that order."*

Over the next three to five years, however, we believe quality mining, energy and agriculture companies with extended competitive natural resource advantages in industries with reasonable natural resource supply constraints will continue to prosper. Our portfolio is structured to reflect this, made up of what we consider high quality companies with a strong business and supportive outlook. Of these, only low cost producers are evaluated for portfolio consideration. In short, we will avoid high-cost producers like the plague.

For further information on Henderson's fund range please contact your local sales office or visit our website:

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