SIA
Strategic Investment Advisors Group

Long Term Investment Fund

Newsletter

of November 2024

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Figure 1: **LTIF Classic EUR**
vs. MSCI Daily TR Net World Index EUR

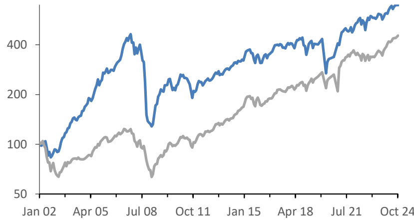

Figure 2: **LTIF Natural Resources EUR**
vs. S&P Global Nat. Res. Net TR Index EUR

"Forecasts may tell you a great deal about the forecaster; they tell you nothing about the future.'"

Warren Buffet

Overview of our funds

Table 1: **Net Asset Value - Net assets under management of our Funds**

October 31, 2024	NAV	Δ 3m	Δ 12m	Annualized return (s.i.)	AUM *(in mio)*
LTIF Classic [EUR]	694.59	1.7%	22.3%	8.9%	109
LTIF Natural Resources [EUR]	166.73	-3.2%	17.4%	2.6%	87

Source: SIA Group

I. 2024: EXPECT THE UNEXPECTED

2024 has been a rather strange year: most stock markets have risen strongly while the world economy has continued to slow down amid a flurry of geopolitical risks. Who could have guessed? Once again, this shows that the economy is not the main stock market driver despite some correlation. In this regard, we recall Warren Buffett's comments on economists, analysts, and other stock market participants' actual ability to predict the future: nil.

We at SIA have a baseline macroeconomic scenario, which we would like to summarize in our *Newsletters*, but we only use this to improve our risk management. In reality, **we are stock-pickers and regard ourselves as long-term investors in businesses within a portfolio built to weather any economic downturn**, targeted at capital protection, and a decent return aimed to be 10-12% per year.

As we mentioned, at the end of 2023 (and even before) there were clear signs of a possible global economic recession, which usually correlates with strong stock market corrections. However, fueled by the post-Covid fiscal support and, mainly, by public investments, the US economy has surprised on the upside, boosting earnings and stock markets. **What we believed would be the end of a very long expansionary cycle (2010-2024) has not happened, and it seems that we are still in the last phase of this cycle.**

There are several very relevant factors suggesting that the global economy is beginning a new acceleration phase: Donald Trump and his fiscal policies (despite the expected tariffs), the interest rate cuts, the improved global liquidity, and China's effort to boost its growth after three years of real estate crisis will, among other factors, accelerate the global demand and economic growth.

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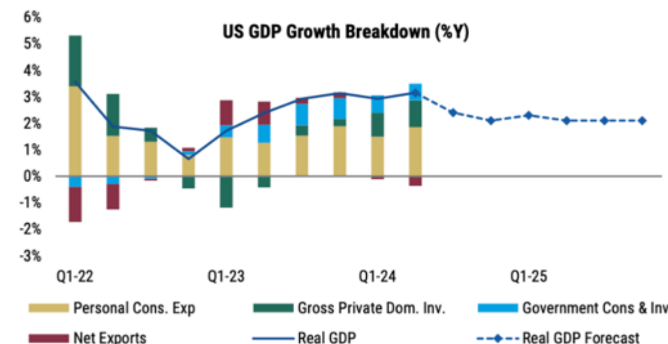
There are, however, also risks that could yet evolve. We highlight three of these. 1) Inflation, which will be under significant upward pressure, following a normalization phase; 2) public deficits/debts, which will require structural measures; and 3) the geopolitical context remains complicated with military and trade wars in a phase of increased confrontation between the East and the West.

We also wonder whether Donald Trump's entrance into the White House will have a positive impact on the war between **the Ukraine and Russia, as well as between Israelis and Palestinians.** We will not provide qualitative assessments, but the chances of this happening are greater now than a few months ago**.**

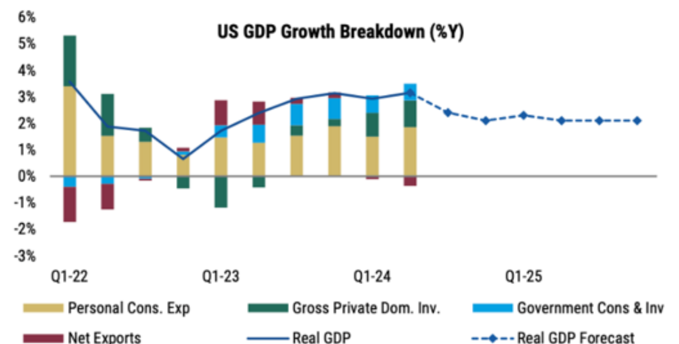
The macroeconomic environment has changed: the global economy is ready to accelerate

The macroeconomic environment has been gradually changing throughout 2024, starting with fear of a possible recession, being constantly positively surprised by the US economy, and ending the year with a new cycle of interest rates cuts. Donald Trump's resounding victory in November completed the puzzle.

All our data suggests that the economies of the US, Europe, and even China are going to start accelerating. We expect the US to grow above 2%, Europe around 1.5%, and China more than its 5% target (see charts below). We are entering a new global phase of economic growth, although, given the starting basis, this growth cannot be too strong.



Source: BEA, Morgan Stanley Research forecasts as of September 06, 2024



Source: BEA, Morgan Stanley Research forecasts as of September 06, 2024

At last a new upward cycle in industrial production

Our estimates also indicate that global industrial production has bottomed out after two and a half years of deceleration and that the destocking phase is coming to an end. We anticipate an improvement in the industrial production cycle in the US, Europe, and China, which normally takes two/three years. Lower interest rates, public investment, investment in energy transition, improvement in the residential sector, and improved consumer confidence (wages, rates) should fuel the next upward industrial cycle. We will have to combat trade wars, which the US is likely to start, but we do not believe that these will be a factor that will jeopardize the new cycle.

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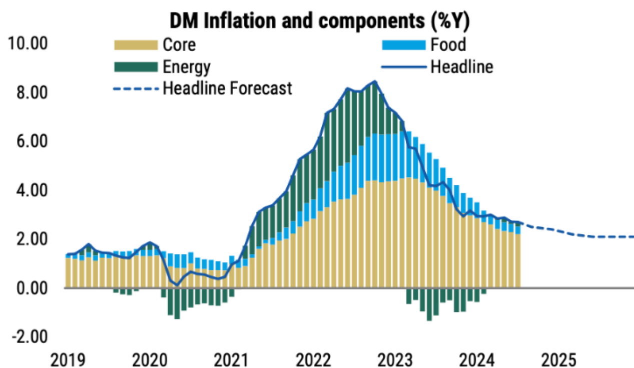
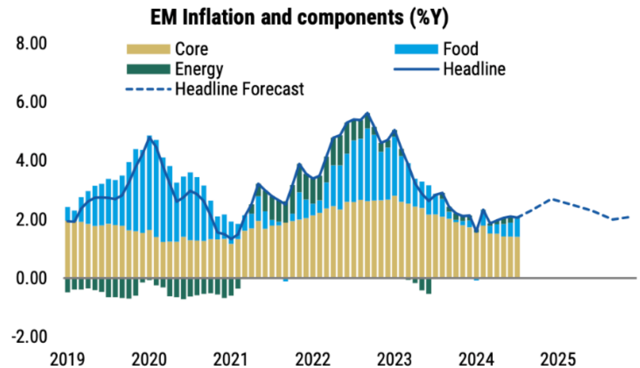
Source: BMO Capital Markets, Haver, Bloomberg. EU industrial production is a BMOCM estimate.

Inflation is approaching a trough; upward pressure is coming; we move to the bearish camp

Inflation is approaching the central banks' targets, which is good news. However, following all recent events, we think that inflation has entered a different stage than the one that started after the 2008/09 crisis. In an environment of labor market shortages and immigration barriers, energy transition, and housing scarcity, we have entered a period of higher structural inflation. In addition, Trump and geopolitical tensions will contribute to higher inflation in the medium term. **Consequently, we believe that inflation is moving toward a new period of clear upward tensions and central banks juggling to get closer to that 2% target, which might even be lifted.**



Source: Haver, Morgan Stanley Research forecasts as of September 06, 2024



Source: Haver, Morgan Stanley Research fas of September 06, 2024. EM inflation excludes Egypt, Turkey and Argentina. China's CPI weights are the ones inferred by Bloomberg

China: marginal improvements

China has recently launched new stimulus plans for the economy (again), which can be summarized as: 1) a more expansionary monetary policy; 2) fiscal support; 3) gradual increase in public investment; 4) restructuring the local government debts and providing permission to issue new bonds; 5) cleaning or completing the housing under construction or finished inventory. We do not know if these plans will be sufficient for a spectacular recovery, but a recovery is just a matter of time. This will happen, because the Chinese Government has the tools to manage it. **We have seen a downward real estate cycle in China during the past 3 years** — a year longer than normally expected.

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The Chinese government has clear long-term objectives and is implementing structural policies step by step to attain them. We highlight just a few of them: 1) technological development that will shift the country from being a low-cost to a value-added producer; 2) greater independence from foreign countries in terms of raw materials and energy; 3) advancing an energy transition aimed at being a leader in the field; 4) evolving from a construction and infrastructure economy to a service/internal demand and technology economy; and 5) upholding the Chinese Communist Party's power.

As the following charts show, the industrial inventories' and the Chinese housing sector's cycles are very low. Although we tend to extrapolate negativity when everything is negative, cycles do come to an end. We therefore think that the Chinese economy will accelerate in the coming years.

Source: National Bureau of Statistics, Bloomberg, CEIC, BMO Capital Markets

Source: National Bureau of Statistics, CEIC, BMO Capital Markets

II. VALUATION UPDATE. IT'S HARD TO BELIEVE, BUT THE MARKETS ARE NOT OVERVALUED

We decided to review the main country and sector valuations in order to not lose our market perspectives given the rise of most stock indices in 2024 and the *Magnificent 7*'s distorting effect. To keep the analysis as simple as possible, we decided to only present the various indices' 2025 P/E, as indicated in the tables below.

At the global level, there are several relevant conclusions:

1) **Value is cheap** versus growth, which trades well above its historical average.
2) **American indices are the most expensive**, above their historical average, but are weighted by the Magnificent 7 and Tech. The SPX500 equal weighted (SPW) is trading at 17.4x, below its long-term average, suggesting that the broad market is not that expensive.
3) **Europe is cheap**, trading at 13x the 2025 earnings.
4) **Emerging markets look very cheap**, but geopolitical issues remain unresolved.
5) By sector, only **Technology is trading at a significant premium** in terms of its historical average, while **Health, Materials, Energy, and Financials are overall trading at a discount.**

1. ***Factors.*** *Value* is clearly cheaper than *Growth*:

MXWO INDEX	***VALUE***	***GROWTH***
PRICE	3.866	5.730
PER 2025	**14,7x**	27,3x
HISTORICAL PER	**17,3x**	23,6x

Source: Bloomberg, MSCI, SIA

2. ***Geographies.*** MSCI regional indices are not expensive by historical standards:

Index	***SPW***	***SPX***	***NDX***	***SXXP***	***SHSZ300***	***BOVESPA***	***TURKEY***	***RUSSIA (*)***	***TOPIX***
Price	7.416	5.973	21.100	510	4.104	129.680	9.100	3.123	2.742
PER 2025	**17,4**	**21,9**	**26,3**	**13,1**	**13,3**	**7,5**	**4,0**	**2,5**	**14,7**
Historical PER	18,5	17,5	25,0	**19,0**	**17,0**	**16,0**	**10,5**	**8,0**	**18,0**

Source: Bloomberg, MSCI, SIA (*) Bloomberg June Estimates. November not available

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3. ***Sectors.*** Technology/IT is the only sector trading above its historical levels:

MXWO Index	*Industrial*	*Staples*	*Health*	*Materials*	*Energy*	*Tech*	*Financials*	*Insurance*
Price	429	284	381	362	262	794	185	194
PER25	**21,0**	**18,6**	**17,8**	**17,0**	**12,5**	**29,1**	**13,8**	**12,4**
Historical PER	20,0	21,0	**22,0**	**20,0**	**16,0**	24,3	14,0	**15,0**

It is surprising that in a context of a global economic slowdown corporate results have remained so robust, leading, on average, to only limited downward adjustments in sales and profits. Ultimately, the slowdown has been mild and without structural issues (neither in the sectors nor in the countries — always on average terms).

It is important to once again highlight the structural change that has been occurring for many years now: **the return on listed companies' (and thus listed sectors') invested capital keeps rising**, **again reaching record highs well above its historical average in 2024.**

These returns on capital depend on the sector structure and the competition. They generally only change very gradually and over the long term with structural or regulatory changes. We therefore do not think that the current high margins and returns are a risk for the stock market, at least not in the short to medium term, meaning that the stock market, overall is not overvalued.

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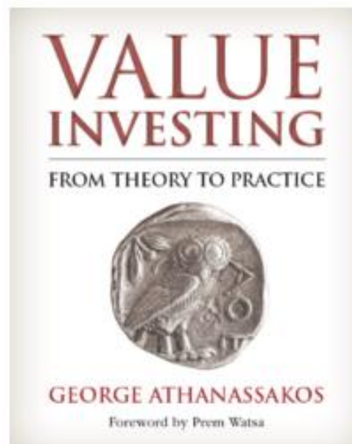
III. WHY IS NOT EVERYBODY A VALUE INVESTOR? *by Alex Rauchenstein*

I was invited to speak at the 4th European Value Conference in Athens on 17 October. Prof. Dr. George Athanassakos of the Ben Graham Centre for Value Investing organized this conference at the Ivey Business School in Toronto, Canada. My gift was a signed copy of Prof. Athanassakos's fascinating latest book called "Value Investing from Theory to Practice".



I think this book, with its links to theory and practice, has the potential to become a classic reference book for any Value Investor, whether a student, an experienced fund manager, a CEO, or a company CFO.

I would like to specifically highlight chapter 1.7 "***Why is not everyone a value investor?***" In this chapter, George explains why not all investors adopt value investing strategies. This is very surprising, given returns' superiority over the long term.

His main points are:

1. **Market Efficiency Belief**: Some investors adhere to the Efficient Market Hypothesis, believing that stock prices already reflect all available information, which makes seeking undervalued stocks a futile endeavor.

2. **Performance Pressure**: Institutional investors may specifically face pressure to provide short-term results, which could deter them from the long-term focus that value investing requires.

3. **Lack of Patience:** Value investing often requires a patient approach, as it could take a long time for the market to recognize a stock's intrinsic value. Many investors lack the patience to wait for these opportunities to materialize.

His main conclusion is:
While value investing has consistently proven its worth, it remains underutilized due to a combination of psychological, institutional, and educational factors. Behavioral biases, one's faith in the market efficiency, short-term performance pressures, impatience, and a lack of knowledge all contribute to it being relatively unknown.

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However, for those willing to overcome these barriers, value investing offers a powerful framework for building long-term wealth. By focusing on intrinsic value and adopting a disciplined, patient approach, investors can navigate market fluctuations, and capitalize on opportunities that others might overlook.

In the end, value investing is not just a strategy; it's a mindset – one that requires resilience, independence, and a long-term perspective. For those who are able to master these qualities, the rewards are immense.

MSCI Value / MSCI Growth (since 1974)

George's book was published in 2022, but as you can see from the chart above, value strategies are still facing the worst possible headwind or, according to some, are dead. But we believe the saying that "those declared dead live longer."

The following is a true story, which I believe fits the discussed topic pretty well: About two years ago, a friend of mine's son wanted to write his master thesis on Value Investing at one of the top Swiss Universities. So, how did he fare? He could not find a professor willing to work with him on this "outdated investment concept." Some professors asked him, who is interested in **value investing** in the age of **AI?**

To me this is a very good example to explain where we are in the current cycle. But will this be the tipping point for the value growth cycle? We do not know, of course. However, it is absolutely clear to me that investors should diversify and should therefore put some of their money to work with a few value managers.

Talking about AI, we are sure that it will revolutionize our world, but be careful that you do not invest in a theme that will never make money for you as a shareholder.

IV. LONG TERM INVESTMENT FUND (LTIF) CLASSIC: +15% ytd. to €710 per share

LTIF Classic is slightly above our 2024 target

At the end of November, nearing the end of the year, **the LTIF Classic is up +15% ytd. to €710 per unit, slightly above our estimates of a normalized NAV of €690 for 2024**. Interestingly, neither Grifols, ISS, and Reckitt Beckinser (23% of the fund), nor Energy and Salmon (25% of the fund) are having a good 2024, which makes us optimistic about the next leg of the fund's performance.

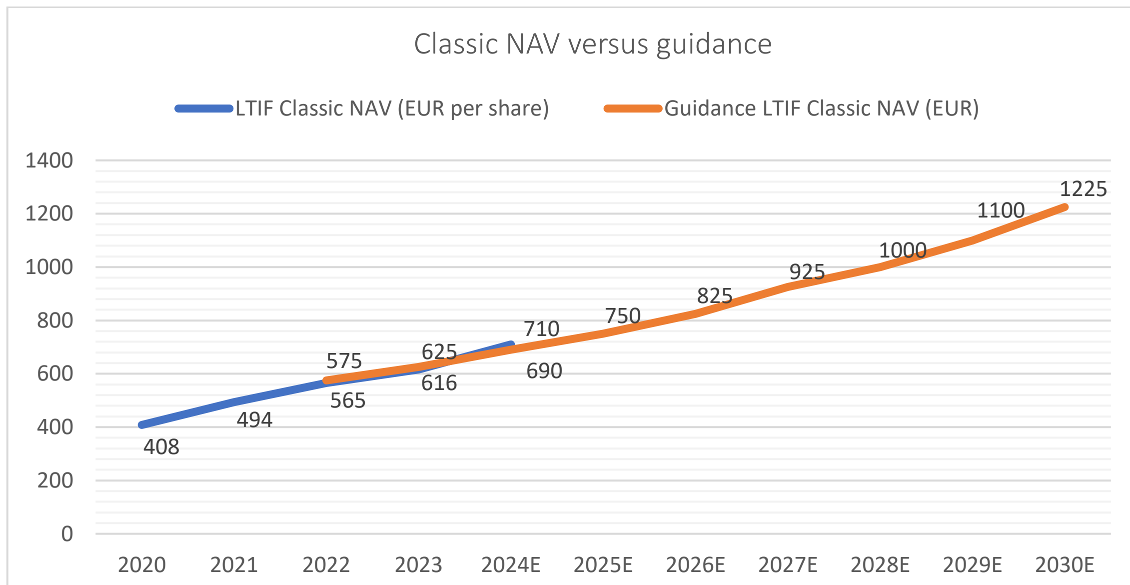
What has been doing well? Power cables, cement, copper, aerospace, defense, business services, and financials provided a strong performance; we have therefore reduced their weightings. Since we usually rebalance the fund based on valuations and risk, we always have a relevant part of the fund from which a lot of value should emerge in the next few years.

The best stock performers were: MTU Aeroengines, Raytheon, Heidelberg Cement, Prysmian, Nexans, and First Quantum. The worst stocks by far were Grifols and Reckitt Beckinser.

The Classic's updated IRR stands at 14,1%, with an Intrinsic Value (IV) of €1035 per share

After the fund's good performance year to date, the updated IRR stands at 14,1% (before fees and expenses), meaning that the net IRR could now be around 12-13%, which is in line with the annual return that we achieved over the last 5 years. We believe that this return is representative of our real potential, given that it includes a major crisis (Covid-19), while the markets are not overall overvalued right now.

Since we started the NAV guidance in 2021, we have not strayed too far from the annual target and could, in fact, exceed it for the first time in 2024. It is good to see that our hard work is bearing fruit.



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If we manage to maintain the average annual return of the last 5 years (12% annual net), we will double the invested capital every 6 years, thanks to the compounding massive power: 1 million euros invested in 2024 will be 2 million in 2030, and 4 million in 2036. **We never tire of reiterating the importance of compounding in the long-term return formula,** something that too many investors underappreciate, focusing too much in the short term and on speculation, with obviously very frustrating results and *post-speculation stress*.

45% of the LTIF Classic is invested in 10 well-diversified stocks

Many years ago, we decided that no single stock/sector/factor's impact would dominate the LTIF Classic's performance, and this decision has mainly translated into two rules: 1) avoid too much weight in any company, sector, or any other risk factor that could become a *black dog*; and 2) half of the fund is invested in about 10 stocks with weights of around 5%, with the aim of simultaneously concentrating and diversifying.

However, when opportunities arise, we adapt, and this is what has happened in 2024: **the LTIF Classic increased the weight of two of its main positions to levels of 8-9% of the fund: Grifols and ISS are the two current "anomalies."**

Generally, we will not deviate from our basic rules, which aim to both concentrate and diversify the investment while controlling the risk. However, occasionally opportunities come along that, in Warren Buffett's words, are huge baseballs coming straight and soft toward the bat. And then we swing hard, as hard as we can *(note that the UCITS regulation does not, in any case, allow us to exceed 10%).*

We are obviously pleased to see that our *mentor* Warren Buffett applies this batting rule whenever he finds interesting investments, because ultimately there are only a few unique investment opportunities like Grifols and ISS, which we discussed in detail in recent newsletters and presentations.

These are the LTIF Classic's main holdings:

LTIF Classic Top10 Holdings (Nov2024)

Grifols SA	9%
ISS A/S	8%
Leroy Seafood ASA	5%
Reckitt Beckinser Plc.	4%
Unilever Plc.	4%
Medtronic Plc.	4%
Henkel AG	3%
Mowi ASA	3%
Grieg Seafood ASA	3%
First Quantum Ltd.	3%
TOTAL	**45%**

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V: THE QUARTERLY INVESTMENT CASE: GRIFOLS

We decided to publish the letter we sent to the Grifols Board of Directors and to the National Securities Market Commission (CNMV) in Spain, explaining our position with respect to Grifols. This letter is not a matter of pride or other strange considerations, it is only a **matter of defending the interests of our investors** (and minority shareholders in general) which is also fundamental for SIA Funds.

Lachen, September 17, 2024

Dear Members of the Board of Directors:

My name is Marcos Hernández Aguado and I am the Managing Partner and CIO of the Swiss fund manager SIA Funds. I am writing to you as a minority shareholder of Grifols, with a position of 1.3 million preferred shares of the company, with the intention of **conveying our concern about a possible offer from Brookfield Capital Partners together with members of the Grifols family.**

1. SIA Funds is a boutique asset manager with 250 million euros under management. **We have 10% of one of our funds** (LTIF Classic ISIN LU0244071956 with assets of 100 million euros) **invested in Grifols' preferred shares, the maximum allowed under UCITS legislation**.

2. **We have known Grifols for a decade and have been shareholders at various stages over the last ten years**. We have gradually bought back shares since the fall of the shares in 2020 and stepped-up purchases since the Gotham Research report was published in early 2024.

3. **For many years, we have been aware of Grifols' historical problems** (communication, governance, accounting, the treatment of minority shareholders, acquisitions, debt, and the effect of COVID-19 on the company's earnings). **Despite this, we found the restructuring plan coherent and decided to support the company by investing heavily.**

4. At SIA Funds**, we believe that Mr. Nacho Abia's new strategy and leadership will bear fruit in the medium term.** Thus, the share price will gradually return to historical levels, which is in line with the strength of Grifols' plasma business.

5. **We were surprised and disappointed by the announcement by Brookfield and the Grifols family to launch a takeover bid for the company,** given that, after much effort, the restructuring and changes are beginning to bear fruit. We are concerned about the **obvious CONFLICT OF INTEREST between the family and the company in the bid**. It

   seems that the Grifols family is not aligned with minority investors who will be disadvantaged by an offer perceived to be very low in terms of the company's intrinsic value. We do not fully understand the benefit of the Grifols family making a joint offer

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with Brookfield that is well below the company's fundamental value, in which they will not buy shares. This is also a concern for us.

6. **We were discouraged by the valuations leaked to the press** (around 12 euros per share), **which seems ridiculous.** We have a detailed discounted cash flow model for Grifols, which, without forcing, leads us to a valuation of the ordinary shares of 29 euros per share (the same as the preferred shares in the event of a takeover bid).

7. As stated in the bylaws, in the event of a takeover bid, the offer for common shares must be the same as the offer for preferred shares. Leaks in the press suggest that the offer will be lower for preferred shares. **We urge you to enforce these bylaws and to discourage offers that would need a change in these bylaws.**

8. Some Grifols documents refer to a multiple of 13x EV/EBITDA as representative of the group's historical average. Some transactions in plasma-related businesses (donation centers) have been carried out around that figure. But considering the EBITDA multiple that Grifols paid for Biotest (over 20x, adjusted), the historical CSL multiple (19.8x between 1994-2024) and Grifols' historical averages (16x), it is easy to see that even 13x is too low. **According to Bloomberg, the historical median (from the IPO to the end of August 2024), the EV/EBITDA of Grifols is 16.3x, more representative of the company's fundamental value**.

   Example of a simple calculation:
   EBITDA 2024E 1,825 million x 16.3x =29,748 million euros.
   Less debt: €9.1 billion after the sale of Shanghai Raas, including leasing. In line with analysts' consensus on the 2024 year-end.
   Equity value: EUR 20,648 million or EUR 30.00 per share (using 687.5 million shares, including preferred shares).
   (*) We have made the same calculations, adjusting the EBITDA and the net financial debt of minority shareholdings (GDS, Biotest, BPC, and HAEMA) and obtained 25.2 euros per share for 2024 and 29.7 euros using 2025 estimates.
   (**) Our DCF (discounted cash flows) sets the value of Grifols at 29 euros per share using a WACC of 10% and terminal growth of 6% (23 euros using 5% terminal growth).
   (***) Using these and other methodologies, our estimated valuation range is between 23 and 30 euros, with an average of 27 euros per share.

9. **We do not want to sell.** We seek to invest in and support Grifols on its path to normality after four years of distress (from 2020, but especially in 2024) that should result in an improvement stage and the normalization of the results, cash flows, and balance sheet.

10. **We ask you to defend the minority shareholders of the 2 share classes and not to accept a price too far from 30 euros per share, which Grifols is fundamentally worth, according to our estimates**. The company's share price was at these levels in early 2020, before the impact of COVID-19 on the group's performance.

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11. **The average analyst valuation** (source: Bloomberg) **is €17 per share, but several (more sophisticated) are at €25. We are sure that many analysts are still too influenced by Gotham Research** and the current negativity around the company, as well as by some incompetence.

12. We are also convinced that **an offer below the share price prior to Gotham's report is,** in the company's (and our) view, totally unjustified, and **would acknowledge that they are taking advantage of the downturn to buy.**

While thanking you for your interest, we urge you to defend the company's minority shareholders by rejecting any offer that significantly undervalues Grifols' intrinsic value.

We remain at your disposal for any clarification you may require.

Best regards

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VI. LONG TERM INVESTMENT FUND (LTIF) NATURAL RESOURCES: +12% ytd

LTIF Natural Resources: +12% year-to-date. EUR 170 per share

LTIF Natural Resources continues battling the odds in the macroeconomic environment of a slowdown in the US, Europe, and in average terms global. **Although commodities tend to do poorly in economic slowdowns, the fund is up 12% through November**, ahead of most commodity indices that very much flat for the year. We are therefore satisfied with the fund's performance this year, which is the fifth consecutive up year.

This year, the best sectors have been Infrastructures (+30%) and Mining (+14%), with Agri-Food up 5%. On the negative side, Energy is experiencing a tough year, and our investments in the sector are, on average, down 9%.

Stocks with gains above 20% are: Suncor, Cameco, First Quantum, Hudbay Minerals, Ivanhoe, Lundin Mining, Southern Copper, Heidelberg Materials, Bureau Veritas, Prysmian, and Nexans. On the negative side, we highlight Woodside Petroleum, AkerBP, TGS, Occidental, and Petrobras.

An IRR of 14%. An intrinsic value of €240 per share

The fund's updated IRR currently stands at 14%, and the intrinsic value at €240 per share, with a two- to three-year appreciation potential of 40% at the mid-cycle valuations. As usual, we insist that the fund's potential is higher than its intrinsic value, given that the commodity cycles reach very high valuation levels, which reflect the difficulty of raising supply in the medium term once the market moves to an undersupplied level.

Our main sector positions are **oil companies (28% of the fund), copper miners (20%), and salmon farms (16%) for a total of almost two-thirds of the fund.** The main positions are as follows:

Top 10 Holdings	***Weight***	***PER26***
First Quantum	5%	9,9
Teck Resources	5%	22 (*)
Leroy Seafood	5%	8,7
Harbour Energy	5%	7,2
TGS	5%	6,3
Atalaya Mining	4%	5,1
Kazatomprom	4%	7,9
EOG Resources	4%	11,3
Occidental Petroleum	4%	11,9
Grieg Seafood	3%	8,8
Total	**44%**	**8,6**

(*) Sold Met Coal Assets to Glencore

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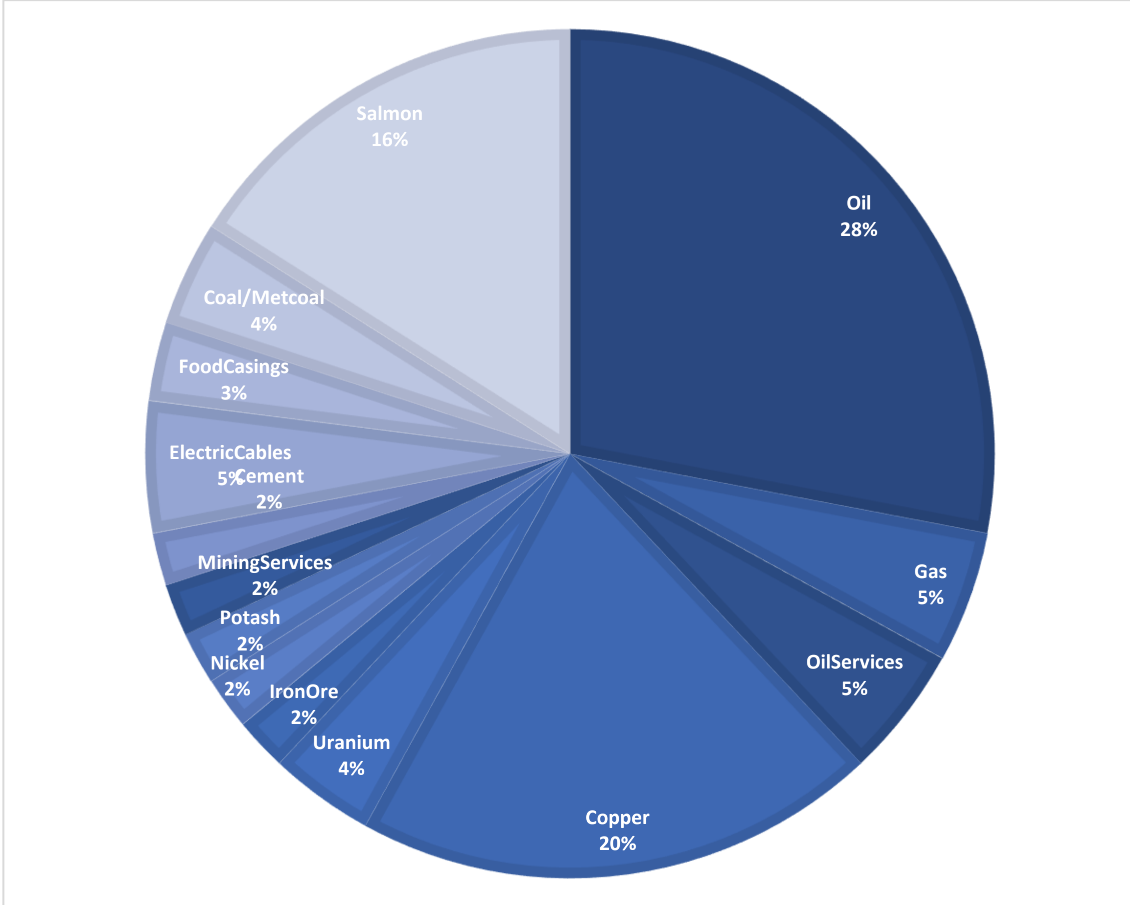
The sector breakdown is as follows:



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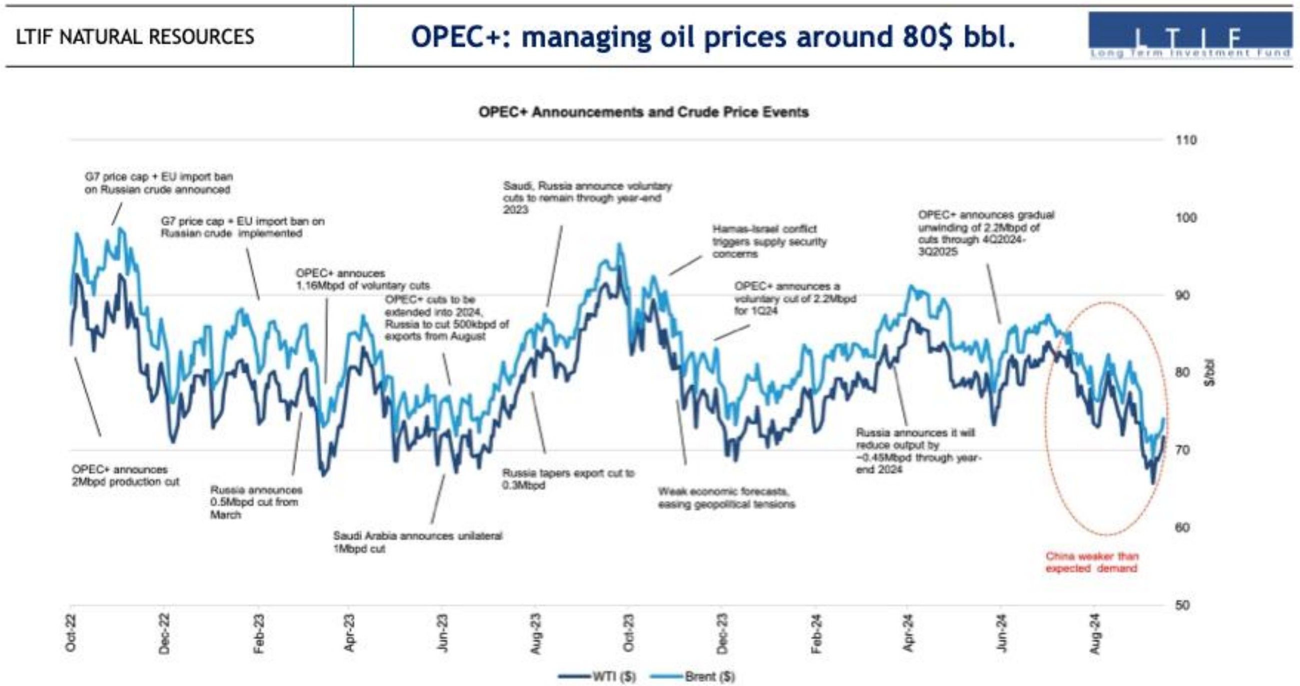
VII. THE OIL MARKET: SO FAR SO GOOD. THE MID TERM LOOKS CHALLENGING

Did you notice that oil has been trading in the $70-100 range for the past two years?

The graph below shows the massive amount of news published about the oil market (several relevant news plus hundreds of rumors/comments are released every day). This news is responsible for the oil prices' strong volatility.

Moving away from this daily news flow (the source of many traders' speculative profits), **we can observe that Brent has been trading in a range between $70 and $100 per barrel, with an average of $84 per barrel, during the last two years.** The reason is simple: OPEC+ turns off the tap (real and virtual/expectations) when the prices approach $70 per barrel, and opens it once the prices are above $90, levels where the US rig count starts reactivating.



Source: Bloomberg, Bernstein analysis

In 2024 the supply and demand have been evenly matched

The crude oil market has been well supplied in 2024, a year in which the expected demand growth was revised down from +1.5m b/d at the beginning of the year to just under +1m b/d, due to the global economic slowdown (including in China).

Supply was also revised down throughout this year, mainly due to US shale, which will grow less than estimated (we estimate a final growth figure of around 300,000-400,000 b/d).

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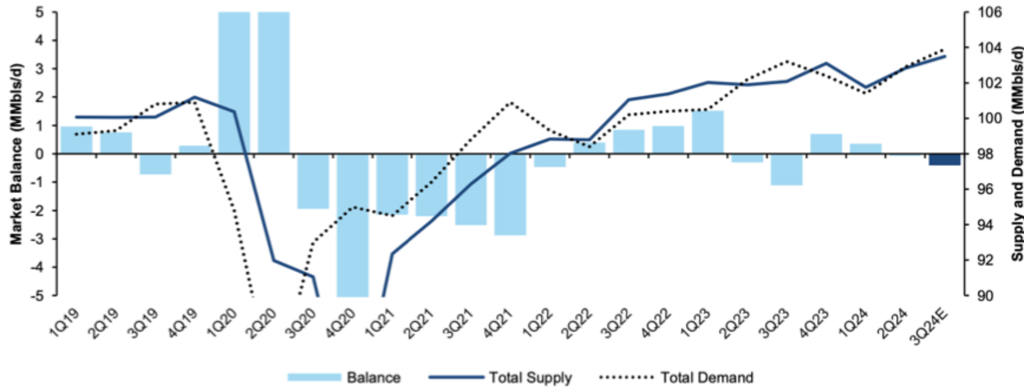
LTIF NATURAL RESOURCES | **2024: a balanced market** | LTIF Long Term Investment Fund

Current situation: small deficit in Q324. Flat ytd



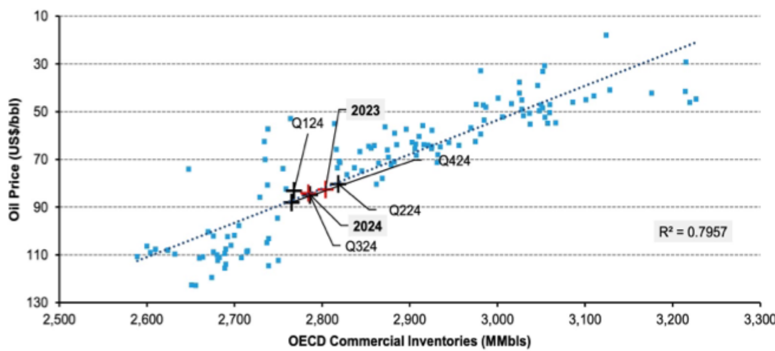
Source: IEA, Bernstein estimates and analysis

3

In summary, **supply and demand have grown in tandem, which has resulted in flat global inventories this year, however, still at low levels compared to the last 5 years' average**. The graph below shows the strong correlation between the OECD inventories and the oil prices, which is working quite well this year.

LTIF NATURAL RESOURCES | **Oil market looks ok for 2/3 years with upside** | LTIF Long Term Investment Fund

High Correlation OECD inventories and oil price



Enough spare capacity and supply for 2024/26. OPEC+ will manage production to keep prices around $80-$90 Brent

Source: Bloomberg, IEA, Bernstein analysis

7

Excess capacity is around 4-5m b/d

We estimate that OPEC+ cuts have brought the sector's spare capacity to around 4-5m b/d, which is ultimately a cushion in case the Israel-Palestine war worsens, or economic growth accelerates. Any sector at 95% capacity is considered full capacity so while it is true that OPEC+ can pump 2-3m b/d in the next 2-3 years to meet demand, **it is also true that idle capacity below 97/98% implies an actual**

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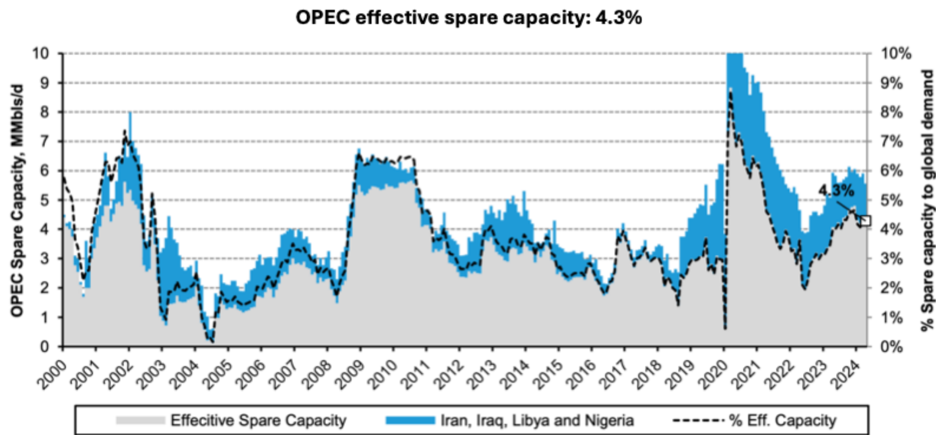
shortage problem. Our numbers suggest that we will be there in 2026/27, depending, of course, on the prices and the economic cycle.

LTIF NATURAL RESOURCES | **Effective spare capacity lower than perceived** | LTIF Long Term Investment Fund



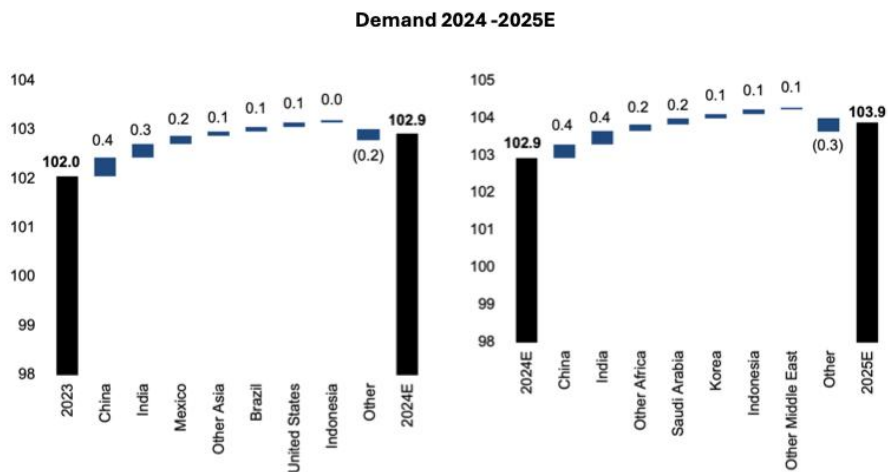
Source: IEA, Bernstein analysis

4

Supply and demand in 2024 and 2025. The supply side doesn't convince us

The graphs below show demand and supply in 2024 and 2025. There is not much debate on the demand side and in years of uncertainty and economic slowdown (in at least 2024 and early 2025) demand will grow by about 1m b/d per year.

LTIF NATURAL RESOURCES | **Demand up 1m b/d within an economic slowdown** | LTIF Long Term Investment Fund

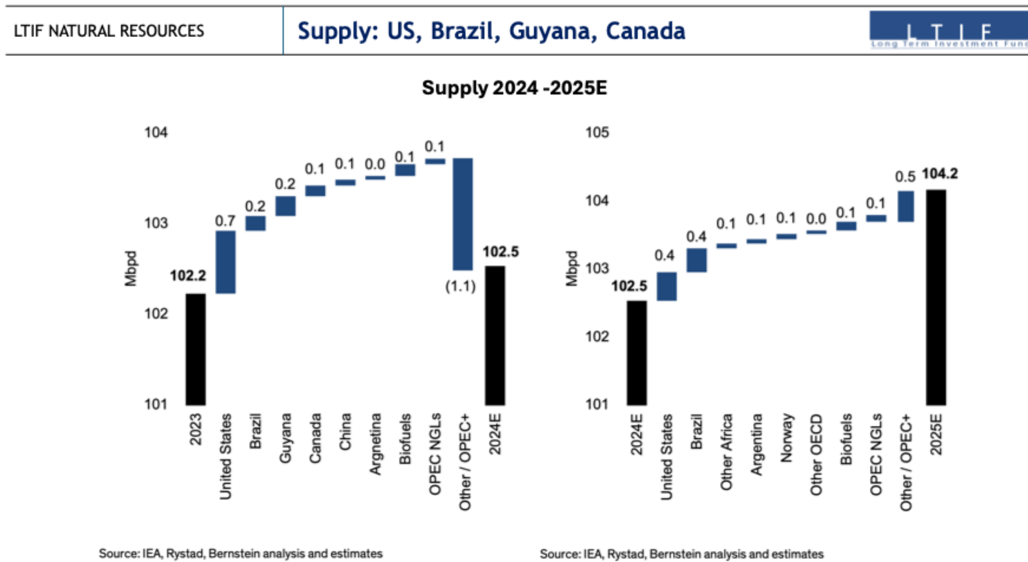


Source: IEA, Bernstein analysis and estimates

Source: IEA, Bernstein analysis and estimates

5

The problem will be on the supply side, because at current barrel prices (Brent $72, WTI $68), US shale is not going to grow since it has been empirically proven that the rig count starts falling below $80 Brent. This leaves supply growth in the hands of Brazil, Guyana, and perhaps Canada, which won't be able to reach 1m b/d on their own, perhaps just 0.5m b/d.



Demand will continue to rise at an average rate of 1m b/d in the medium term

This is the part of the equation where we find the largest discrepancy with our thesis: there is a clear consensus that electrification will kill the demand for oil quite soon, which, according to our numbers, is, however, wrong.

To summarize our thesis in short: three factors predict that peak demand will not be reached until well into the next decade: 1) four-fifths of the world's population is still in a development phase and therefore not ready for electrification, which will take decades; 2) demand in 3 of the 4 demand sectors (aviation, heavy transport, and chemical) will continue to grow in the medium term; 3) our electric car penetration model suggests that gasoline demand will not peak until 2035 at the earliest, due to the slow pace of change in vehicles' installed base.

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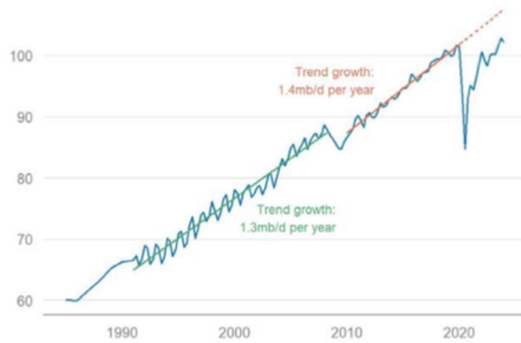
LTIF NATURAL RESOURCES | **Fear of Peak Demand: baseless for 15 years** | LTIF Long Term Investment Fund

Global oil demand - long-term trend
(mb/d)



Source: IEA, Morgan Stanley Research

Demand will continue to grow by 1m b/d in the mid term:

- Of the 5 parts of the world with around 1.5 billion people, 4 will continue to grow.
- Of the 4 end-demand sectors, 3 will continue to grow: Jet Fuel, Chems & Diesel.
- Our EV penetration model: peak demand for gasoline will not occur until 2035.

EXXON: more than 100m/d by 2050

8

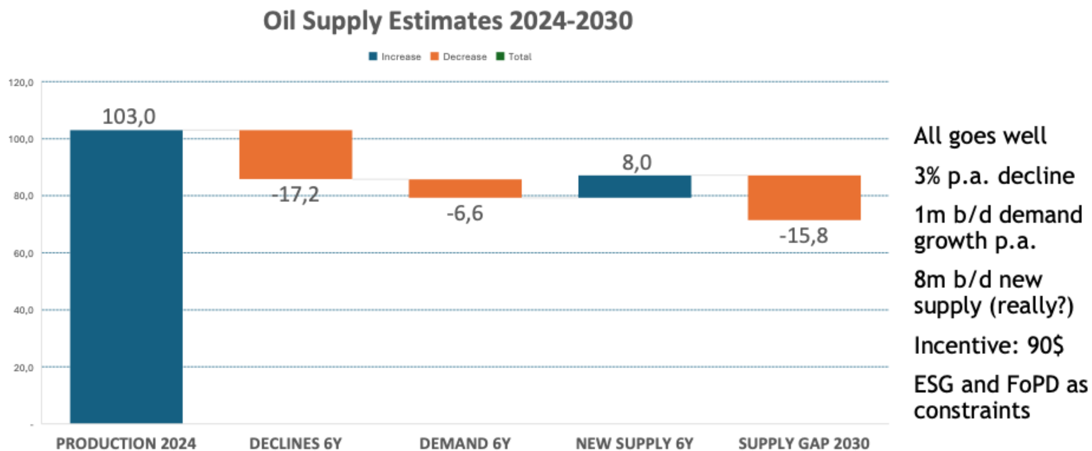
Where will we get 16m b/d by 2030?

The numbers are obvious: in the next 6 years (target 2030) we will need to replace about 17m b/d due to the average decline in production (3% per year) and will have to meet about 6m b/d of the cumulative increase in demand. Therefore, we will need a new production of 23m b/d in total, while oil projects are only being developed for 8m b/d, according to our estimates. This sounds bad.

Even if we would use an extremely low decline (again being very conservative by using the OPEC countries' estimated decline of 1% per year), we would need 12m b/d of new supply, well above our new supply estimates of 8m b/d.

In conclusion, since **the real problem remains unchanged, as does the lack of investment, we are absolutely convinced that we are heading toward a structural deficit in the oil market**.

It is rather surprising, but, from a theoretical point of view, this is precisely what the world needs to curb demand and accelerate the energy transition: a higher oil price to incentivize substitution and electrification.



Who dares to invest in oil?

We reiterate that the most worrying of all is the lack of investment in oil since 2013 (see graph below), the year in which the global investment in oil and gas reached more than 700 billion dollars compared to the current investment of about 500 billion. Both of these are nominal figures.

We summarize the lack of investment in the sector as an idea that we often repeat (perhaps too often) for its simplicity: **the world oil market has been sufficiently supplied and therefore reasonably priced thanks to shale oil,** which produced practically nothing in 2013 but contributed 10% of the world's supply in 2023 (about 10.5million b/d, i.e., equal to Saudi Arabia's production).

But after 10 years of growth (in fact, more than 70% of the growth in the world's supply), shale oil is already a mature sector with no significantly predicted growth in the future. In other words, in the next 10 years we will need to find a new shale, or a new Alaska, or a new North Sea, as well as the approximate $300 billion to finance these.

For the time being, we at SIA are unable to identify new oil resources with enough scale. What is worse, very little is being invested in exploration and development. Why? Fear of peak oil demand, CO_2 emissions, ESG, taxes, geopolitics; in short, a high risk not covered by the returns that the current prices could generate.

In fact, the world has been quite lucky to find/develop shale oil. Without shale, oil prices would undoubtedly have skyrocketed, fueling a new investment cycle, and lowering the demand and economic growth for some time. We believe the latter will happen in 2-3 years, once the current spare capacity has been absorbed.

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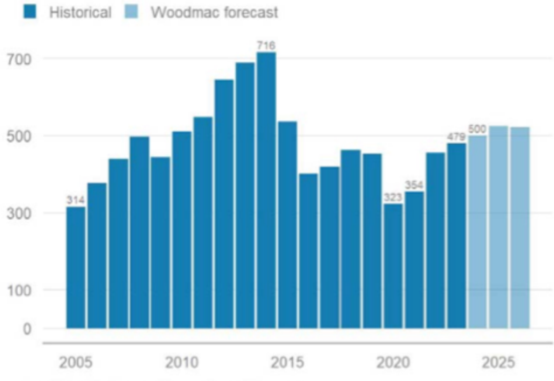
LTIF NATURAL RESOURCES | **Supply. Chronic underinvestment** | LTIF Long Term Investment Fund

Global oil & gas capex
($bn)



Source: Wood Mackenzie, Morgan Stanley Research

- **Lack of upstream capex since 2013.**
- **Well-supplied due to shale oil,** which produced nothing in 2013 and accounted for 10% of the supply in 2023.
- **After 10 years of growth, shale oil is mature.** We need to find a new resource and $ 300bn.
- **We are unable to identify such new oil resource, and little is invested** in exploration and development.

Q1? oil prices if US shale oil had not been found?
Q2? What if we do not find another shale oil?
Prices > 150$bbl on inelasticity

Upstream spending 2025-2026E

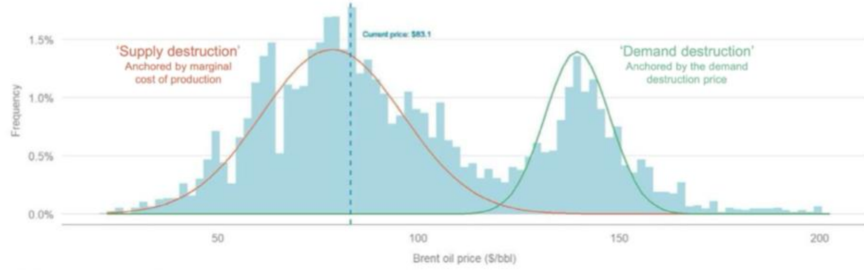
9

Prices will range between $70 and $100 per barrel for a couple of years more

The graph below shows what we expect prices to do in the next 2-3 years. As long as there is spare capacity in OPEC+ (about two years), prices will remain in the range of the first distribution (average Brent around $80/$85). When we reach an idle capacity of 3%, we will move to the distribution on the right with average prices of $140, which will have a negative impact on the demand.

LTIF NATURAL RESOURCES | **Statistical (and real) view on oil prices** | LTIF Long Term Investment Fund

Distribution of inflation-adjusted oil prices
Based on Brent crude oil since 2007 (in 2024 US$/bbl)



Source: Platts, Bloomberg, Morgan Stanley Research

11

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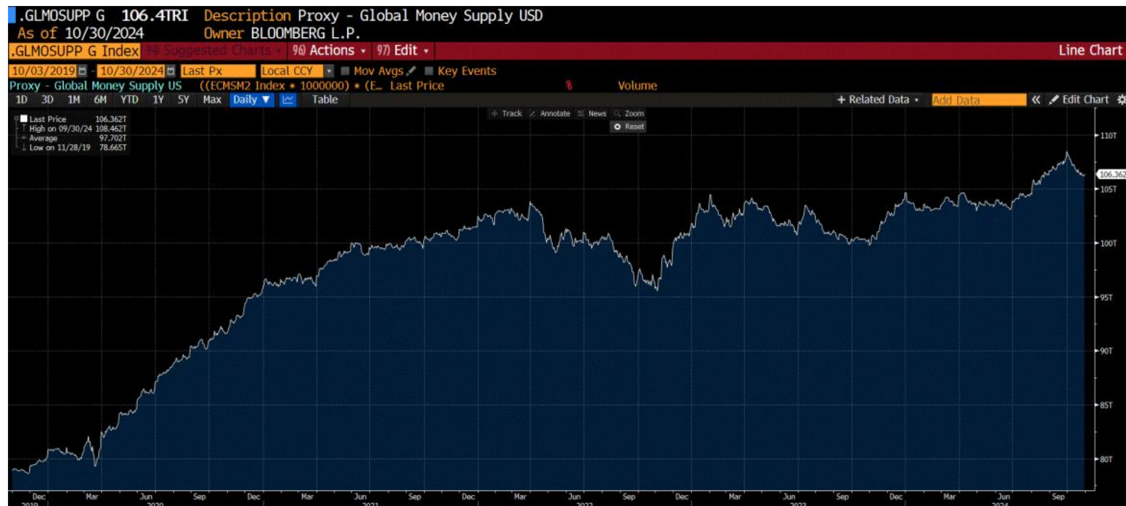
VIII. NATURAL RESOURCES THOUGHTS *by Urs Marti*

Money, money, money

After 3 years of consolidation, the global money supply (M2) broke out on the upside with global policy makers being forced to abandon their relatively hawkish policy.



The public sector's financial situation (the deficits/debts) is problematic, particularly in the West.

In our view, higher interest rates will only be tolerated for a limited time span. Given debt's duration, it takes some time until higher rates lead to a large increase in the amount that needs be spent on serving this debt.

Nevertheless, this time has now arrived. To make matters worse, higher rates lead to a slower economy and a steep decline in tax revenues. Since net exporters then no longer want to invest their trade surplus in the Western bloc's debt, Western central banks are forced to absorb the increasing debt by means of their printing presses.

Gold is always the indicator that smells this change first, everything else follows later. There is a time lag before the growing liquidity reaches the street, and inflation starts increasing again.

Covid created a typical whipsaw effect on the global economy. Everybody was afraid of inflation, global supply chains, and of not having sufficient raw material inventories, and half and finished products. This resulted in a build-up of inventories and overconsumption. Consequently, central banks became more hawkish, the economy slowed down, and inventories had to be decreased.

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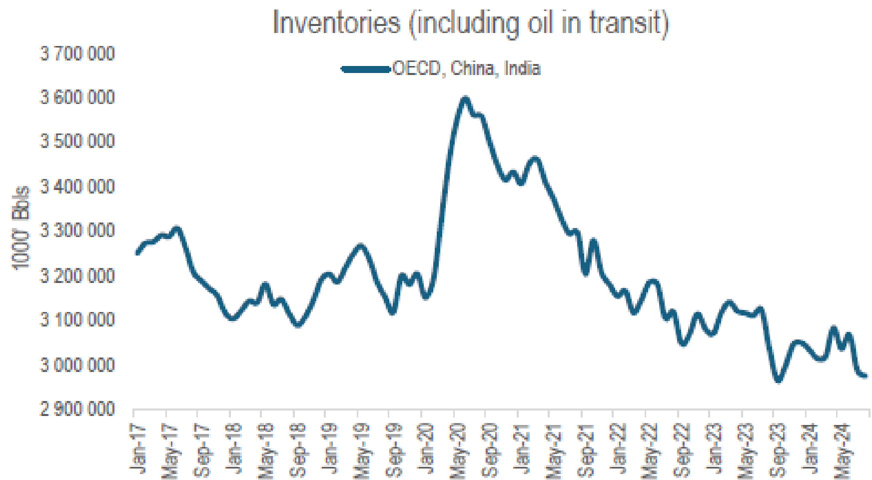
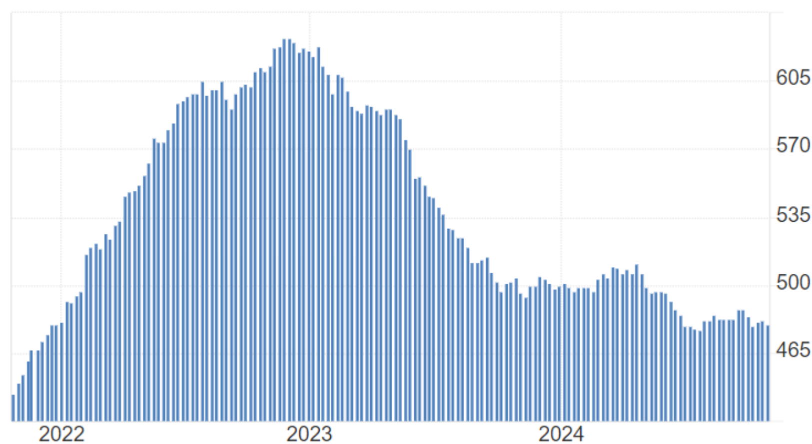
The current situation in the oil market is a good proxy:



Since 2021, investors' mood regarding natural resources, emerging markets, and other "cyclical" sectors has shifted from being very optimistic to being as bearish as it can be.
Oil's financial market participants have never been more exposed to the short side, which means commercials' positions have never been so long. Normally, it is the other way round, since commercials, given their production, which is partly hedged with that of futures, have a structural long position. The combination of depleted inventories and rising global liquidity is an explosive set-up that could lead to similar moves as those recently seen in respect of cocoa.

After three years of correction/consolidation, many commodity prices are now too low, leading to declining production. An example is the USD 120 oil, which led to an increase in drilling activity, as shown in the US crude oil rig count:



Working rigs, which were correlated with the oil price correction, declined and after the usual time lag, the output of US oil stopped growing; it will remain sluggish in the foreseeable future. Higher prices are needed for stable/increased output. (In a recent report, Standard Chartered concluded that

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global demand hit an all-time high of 103.8m barrels p/d in August. Contrary to many pundits' wisdom, a market is obviously in deficit when global inventories decline, not when the opposite occurs.)

The oil market situation applies to many other markets like those of potash, metals, salmon, and PGMs.

BHP has shut down the nickel business in Australia, while Chinese investments in Indonesia are decreasing. Copper treatment and Chinese smelters' refining fees have seen a sharp reduction to $23 per metric ton, which is down from $80. TC/RC is a gauge of the availability of copper concentrates used in refined copper's production. A lower charge signals shortages/the tight supply of mining products. The situation is similar in other metals like zinc, which is again in backwardation (despite the still sluggish economy). On the other hand, Antofagasta issued a fresh warning about the "disconnect" between government policies not issuing permits for new mines quickly enough, and about the demand for the metal. The world needs to add the equivalent of Chile's entire copper production over the next decade.

The whole ESG/energy transition bubble continues to deflate.
The energy transition is a massive structural change that will take many decades before it is completed. However, its start was a massive ideological manipulation with many targets not based on science or physics.

The newest victim is hydrogen due to the hype having to face a reality check at last. Stocks crashed and the excitement has faded due the lack of economic benefits. Major energy companies, like Shell and Equinor, have scrapped their investment plans. BP is another company being brought to its senses – but only after wasting billions and billions of shareholders' money. Structurally, it is very bad for companies if they are managed by politics and ideology.

In mining, Anglo is a similar example; it's one of the worst managed mining companies, which planned to sell its coal business for ideological reasons, the PGM business is currently at an all-time low, with other businesses following this pattern.

Glencore, owned by clever partners, has been doing the opposite and has snapped up unloved coal assets all over the world for years, paying multiples of 2-3 times EBITDA. The company is also interested in obtaining Anglo's good coal assets. Contrary to the propaganda, coal is still king and on its throne despite the transition push. It provides cheap and reliable energy, and remains the largest source of electricity. Even the IEA has admitted that the demand for coal is not about to decrease, despite its projections that wind and solar growth would see the demand for all hydrocarbons decline before 2030, nor will it decline after 2030.

Given the described developments and subsequent relative valuations, the fund continued to increase its exposure to the oil/fossil fuels sector. In addition, the fund added exposure to large mining companies like Rio Tinto, BHP, Glencore, and Nutrien at very attractive valuation levels.

Approx. 80% of the world's iron ore supply originates from Western Australia and Brazil. Rio and BHP account for the major part of Australia's production. All these mining companies possess some of the world's best assets, for example, the world's largest copper mine, Escondida. Glencore and Teck are the world's largest producer of zinc/lead concentrate. Glencore is the world's largest exporter of coal and, since the deal with Teck, in control of the majority of seaborne high quality metallurgic coal with BHP.

Glencore is one of the world's largest and lowest cost producer of ferrochrome/vanadium, and the world's largest cobalt producer. Rio Tinto's Richard Bay is a world leader in heavy mineral sands' extraction and refining. Rio Tinto is a global leader in aluminum, with a large-scale, vertically integrated

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business: Bauxite mines and alumina refineries as well as smelters producing aluminum. Similar to other commodities, Chinese port inventories have been depleted, and the disruption of Guinea's exports have recently resulted in an Alumina price spike from US$330 to US$700 per ton.

Marcos Hernández Aguado
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SIA Team

November 2024

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