MARKET COMMENTARY

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SPRING 2018 RESOURCE MARKET OUTLOOK

Normally at this late stage of the business cycle, the leadership baton would have been passed on to the sectors that benefit the most from robust economic growth, yet for the Resources sector, the transition has been at best half hearted. Selective commodities have enjoyed market support, such as metals related to the electric car craze like cobalt and lithium. But for the most part, the strength has been sporadic and largely not reflected in resource stock performance. The question is: will the market catch on to a "normal" resource cycle, or will the cycle of the past be bygones?

"...at its 10th year of recovery, the global economy looks to be sustaining its pace"

Come to think of it, being Canadian has been pretty tough for a while. With our major partner the USA taking a hard line on trade negotiation, the usual boost from a strong US economy is diminished and its future much in doubt. Our governments aren't exactly practising prudent fiscal management either, running large deficits when the economy is arguably running near peak speed. Whatever the reasons, our failure to open up better access for our natural resources to a broader market is costing Canada tens of billions of dollars every year, robbing our financial markets of much needed foreign investment. Case in point, in both crude oil and natural gas, the gap between domestic and world prices has increased sharply, depriving our country of wealth and jobs. The prospect looks pretty grim so far.

But there is hope. Even at its 10th year of recovery, the global economy looks to be sustaining its pace, buoyed by the US tax cut and the continuing low interest rates worldwide. As unemployment rates decline while inflation stays subdued, it's the best time for companies to thrive, and corporate earnings show it. Baring a sudden flare-up of inflation, or a major geopolitical miscalculation, the cycle looks good for at least a couple more years. The recent pickup in market volatility also started to drive some money away from the "Nifty-Five" of technology stocks into other sectors. The Resource sector, I believe is set to be one of the beneficiaries as valuation levels remain low after a long period of investor apathy.

Within the resource sector, gold has been fairly steady amid threats of geopolitical unrest, balanced by the unfavourable impact of somewhat higher interest rates. The much hyped crypto currency though is suffering from the inevitable bust after its eye-popping boom, proving that there is a place for a store of value which has proven itself for thousands of years. This is set to continue. Electric metals have seen very good runs, and some of them are overstretched, but future demands look bright. Some of the base metals such as copper and zinc have done well but are not stable at high levels, while others such as nickel is just starting to regain its footing. Ditto for iron ore and coking coal, which had supernova gains, pulled back and are now staying at higher than historical levels.

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In the oil market, the ongoing production cuts by OPEC and non-OPEC producers have finally started to bear fruit with inventories falling sharply. With better crude oil prices, the US shale oil production has bounced back strongly. But even the staunch skeptics such as the International Energy Agency, which previously had a "lower for longer" take, are now worried about the lack of non-OPEC investments outside the US and whether the world is ready for any disruption to oil supply. Demand, on the other hand, continues to be very strong and continues to force the estimates higher. As visible stockpiles in the US, the largest consumer of oil, keep falling, higher oil prices have followed. The uranium production cuts announced by Cameco and Kazatomprom, two of the biggest producers in the world, should go a long way of shaking the buyers out of the slumber and begin to secure long term supply.

Even though all the starts and stops can be very frustrating, the recovery in the resource sector has clearly taken root. The key here really is to be selective and focusing on commodities that have their best days ahead of them, while picking companies which can prudently manage their abundant cash flow and grow organically. The winners will continue winning.

FUTURE STRATEGY

After a long unrelenting bear market, commodities, and by extension resource stocks, have started a recovery process; however uneven and volatile it may be. Given the hopeful signs evident in various commodities, the Manager expects a selective rebound for commodity stocks in the next 12 to 24 months. We will remain cautiously optimistic and seek to add exposure in times of volatility. The current focus of our funds will be low cost oil, uranium and selected metals. We will also continue to high grade the liquidity and safety of our portfolios.

We thank you for your continuing support.

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Maple Leaf Short Duration Flow-Through Limited Partnerships
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