Franklin Gold and Precious Metals Fund

Franklin Templeton Investment Funds

A (acc) USD
31 August 2020

Fund Commentary

Performance Review

- In the first monthly loss since March, spot gold prices edged down from record highs above US$2,000 per troy ounce and ultimately fell 0.4% in August (to US$1,968) despite US jobless claims and other data that reinforced investors' fears of a slower recovery from the coronavirus-induced economic crisis, which dented the US dollar and US Treasury yields. The US dollar's value remained in a weakening trend, particularly against G10 currencies, which boosted price support for dollar-denominated gold bullion. Despite gold's August doldrums, optimism about progress in vaccine development and strength in equities, investors were still searching for hedges—gold has seen a surge in demand lately amidst increased investor anxiety about ever-larger Treasury auctions, ballooning government deficits and the potential for an inflation spike given the unprecedented nature of the US Federal Reserve's latest stimulus moves. Many investors saw better value in silver, which jumped 15.4% to US$28.14 an ounce. To a lesser extent, platinum (+2.9%, to US$950 an ounce) and palladium (+7.4%, to US$2,300) also advanced, as did copper (+4.0%, to a 26-month high of US$6,667 per metric ton) and all other major industrial metals except for tin. Low inventories and supply snags tied to disrupted production at some major mines were key factors supporting copper, iron ore and other non-precious metals.
- For the month, the fund's A (acc) USD shares returned 0.77%, and its benchmark, the FTSE Gold Mines Index, returned -1.36%.

ONE-MONTH KEY PERFORMANCE DRIVERS

	Stocks	Industries
HELPED	Chalice Gold Mines (Off-Benchmark Exposure)	Gold (Stock Selection)
	Red 5 (Off-Benchmark Exposure)	Precious Metals and Minerals (Off-Benchmark Exposure)
	Pretium Resources (Overweight)	Diversified Metals and Mining (Off-Benchmark Exposure)
HURT	Barrick Gold (Significant Underweight)	—
	Agnico Eagle Mines (Significant Underweight)	—
	Alacer Gold (Off-Benchmark Exposure)	—

- Company-specific improvements resulted in major rallies for several of our Australia-based holdings. Exploration focused Chalice Gold Mines' portfolio includes the Pyramid Hill Gold project and two non-gold projects targeting a mixture of copper, nickel, platinum group elements (PGEs) and cobalt. The company's share price rose more than 50% in August as it continued to rapidly advance high-grade PGE/nickel/copper/cobalt discoveries amidst positive preliminary metallurgical testing at its Julimar project, with the latest drill intersections revealing significant extension of three high-grade zones on the property. Drilling activity at Pyramid Hill also yielded some promising results across several gold zones as Chalice continued to define the extent of the overall resource.
- While many gold-mining companies came under selling pressure in August, the portfolio's platinum- and palladium-focused holdings in the precious metals and minerals industry posted strong average gains (including key contributors Northam Platinum and Impala Platinum Holdings), as did our positions in copper-focused and diversified metals and mining companies (led by key contributors Ivanhoe Mines, RTG Mining and Orla Mining). When combined, these off-index investments comprised nearly 16% of the overall portfolio and proved highly beneficial as they outperformed the benchmark.
- In contrast, the fund's relative returns were hindered by substantial declines for some of our off-index or overweighted exposures in the gold industry including Alacer Gold, Perseus Mining, Lion One Metals, Galiano Gold and Torex Gold Resources. In particular, although Alacer Gold reported strong second quarter results, the shares underperformed amidst slower-than-expected approval from the Turkish government's sign-off on their proposed no-premium merger with SSR Mining (not a fund holding) and weaker than expected 2Q20 results from SSR Mining due to temporary COVID-19 related costs and mining delays.

Outlook & Strategy

- After hitting a new all-time intraday high of US$2,075 on 6 August, gold prices pulled back and ultimately consolidated around 31 July closing levels. Physical gold held globally by exchange-traded funds (ETFs) increased by 1.01 million ounces during August, bringing total holdings to 108.9 million ounces—a new high that was well above the previous cycle peak of 82.7 million ounces back in December 2012.
- According to the World Gold Council's second-quarter 2020 review (released in August), 2Q20 gold demand was down 11% on the back of weak jewellery sales and slower central bank purchases, offset somewhat by robust ETF demand. Central banks continued to be net buyers, but their 2Q20 purchases of 114 mt were down 50% from the same period in 2019. Total supply in 2Q20 was down 15% from 2Q19 on the back of a 10% drop in mine supply, an 8% drop in recycled gold, and net producer hedge buybacks in the quarter. Virus-related mine supply disruptions helped keep the market tight despite the very weak jewellery demand.
- Gold averaged US$1,905 in July and August, once again setting the industry up for continued quarter-over-quarter gains considering the US$1,714 per ounce average for the second quarter of 2020. Operationally, most of the mine disruptions experienced in late winter and early spring were due to various government measures to slow the spread of COVID-19. Most of those operations are now back near full capacity (although with slightly higher cost). So far, gold prices have moved up much faster than costs, allowing margin expansion while providing a strong start for gold mining companies' third quarter 2020 results.

- Gold has been performing well, but we still see a number of potential drivers that could move the metal even higher. In our view, gold may benefit from bouts of elevated market volatility and concerns over the impact of the coronavirus as investors seek perceived safe-haven assets. Gold has a very low correlation with other asset classes, supporting increased interest in gold as a portfolio diversification tool. That said, gold often declines with other assets in a true crisis as investors sell all assets to increase liquidity—but gold also frequently holds up better and recovers sooner than other financial assets under such circumstances, just as we experienced this year given the March sell-off and spring recovery.
- Gold equities remain closely correlated to gold bullion, but with higher beta, continuing a trend seen over the past few years. Many gold-focused companies struggled to generate free cash flow in a US$1,250-per-ounce gold environment as total costs for many producers are close to that level, according to our analysis. Mining costs tend to be relatively fixed, so higher gold prices can flow straight to the bottom line, and the move above US$1,900 should provide a very significant lift in cash flow across the industry.
- Following a very active phase in late 2019, new merger-and-acquisition (M&A) activity was muted in 1Q20 but increased in 2Q20 despite the COVID-19 overhang. Endeavour Mining (previously held by the fund) closed its acquisition of Semafo (a fund holding) in July, and Guyana Goldfields closed the takeout by Zijin Mining at the end of August. Meanwhile, TMAC is still awaiting final approval for its acquisition by Shandong Gold (both are fund holdings). Alacer Gold (a fund holding) and SSR Mining are also awaiting final approvals for their no-premium merger of equals that will create a global multi-mine effort based in Denver with operations in Nevada (USA), Canada and Turkey. Given several years of underinvestment by the gold industry, we expect further M&A activity in the months ahead, although the pace could be slowed in the near term by travel restrictions and other short-term business impairments associated with the pandemic.
- We continue to see attractive opportunities in gold- and precious metals-focused equities, especially if gold prices can hold current levels or move even higher. Even when we factor in the strong share-price rebounds from March's lows, many gold companies have seen their forecasted cash flow increase faster than their stock prices over the past year, resulting in contracting equity valuation multiples despite the improving fundamentals. With gold moving even higher and input cost pressures subsiding on the back of lower fuel prices and favourable currency movements in many parts of the world, the compressed valuations make gold equites look even more compelling to us now. Most mining companies have maintained a focus on improving the cost structure of their operations, debt repayment and asset rationalisation, which we believe should result in better businesses and improved stock performance potential going forward as management teams look increasingly focused on turning higher gold prices into free cash flow that can be reinvested in high-return projects (or returned to shareholders via dividends). In addition, we believe small- and middle-capitalisation gold equities may present some of the best opportunities given their generally lower valuations and the industry's recent uptick in M&A activity, which has been receiving a boost as mining companies seek to replenish their resources following several years of limited exploration and development activity.

Fund Details

Inception Date	30/04/2010
Benchmark	FTSE Gold Mines Index

Fund Description

The fund seeks capital appreciation by investing at least 80% of its net assets in the securities of companies around the world that mine, process or deal in gold and other precious metals such as platinum, palladium and silver. The fund has a secondary goal of current income.

Performance Data

Performance Net of Management Fees as at 31/08/2020 (Dividends Reinvested) (%)[1]

	1 Mth	3 Mths	YTD	1 Yr	3 Yrs	5 Yrs	10 Yrs	Since Inception
A (acc) USD	0.77	31.49	42.99	49.52	17.90	19.65	-2.87	-2.31
Net of Sales Charge - A (acc) USD	-4.27	24.92	35.84	42.05	15.90	18.44	-3.36	-2.80
A (acc) SGD	-0.13	26.62	44.44	46.62	18.06	18.76	-2.83	-2.38
Net of Sales Charge - A (acc) SGD	-5.12	20.29	37.22	39.29	16.06	17.56	-3.32	-2.86
FTSE Gold Mines Index USD	-1.36	24.01	47.81	45.41	21.66	27.86	-1.00	-0.42
FTSE Gold Mines Index SGD	-2.20	19.29	49.45	42.52	21.71	26.92	-0.97	-0.50

Investment Team

Steve Land, CFA
Years with Firm 23
Years Experience 23

Fred Fromm, CFA
Years with Firm 28
Years Experience 28

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What Are the Key Risks?

The value of shares in the Fund and income received from it can go down as well as up and investors may not get back the full amount invested. Performance may also be affected by currency fluctuations. Currency fluctuations may affect the value of overseas investments. The Fund invests mainly in equity and equity-related securities of gold and precious metal companies in both developed and emerging countries. Such securities have historically been subject to significant price movements, frequently to a greater extent than equity markets globally. As a result, the performance of the Fund can fluctuate very significantly over relatively short time periods. Other significant risks include: foreign currency risk, emerging markets risk, liquidity risk. For full details of all of the risks applicable to this Fund, please refer to the “Risk Considerations” section of the Fund in the current prospectus of Franklin Templeton Investment Funds.

Important Legal Information

Franklin Gold and Precious Metals Fund is a sub-fund of the Luxembourg-domiciled Franklin Templeton Investment Funds (FTIF).

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