

MG Alpha Return Portfolio

(Separately Managed Account)

SMA Update 31 March 2023

SMA FACTS

Investment Objective: To outperform the benchmark over a 5 to 7 year time horizon by seeking out investments trading at a discount to their intrinsic value. The objective is not a forecast, nor are returns guaranteed.

Investment Strategy:

- Use qualitative and quantitative analysis to seek out value.
- Focus on value investing, indiscriminate of income or growth.
- Diversification when value opportunity is most apparent.

Benchmark ASX200

Indicative no of securities 20

INVESTMENT MANAGERS

Ben Morrissey

30 years investment experience. Lead investment manager and founding advisor for the Morrissey Group.



Alex Henderson

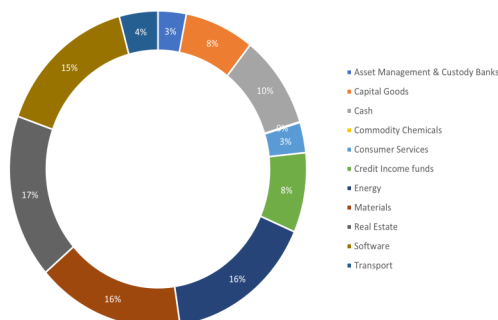
10 years investment experience. Formerly of Goldman Sachs J.B. Were, and current Morrissey Group Model Manager.



TOP 5 PORTFOLIO POSITIONS

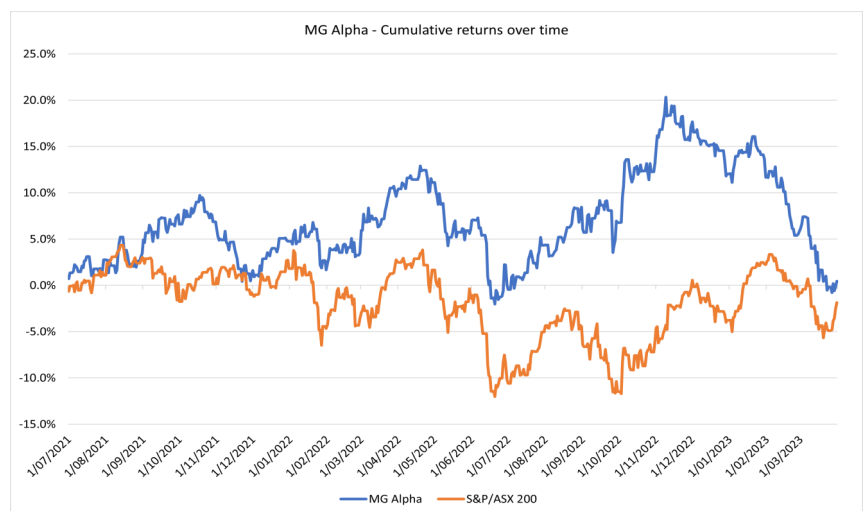
IOD	IODM Limited
WDS	Woodside Energy
GDI	GDI Property Group
Cash	Australian Dollars
WHC	Whitehaven Coal

Industry Sector Weighting



Off the mark

The MG Alpha Return portfolio fell **10.34%**, whilst the **ASX200** rose **1.98%** in the March quarter. The underperformance can be attributed to three stocks; Jervois Global (JRV), IODM (IOD) and Whitehaven Coal (WHC). For JRV and WHC falling commodity prices caused the large falls, and for IOD there was a small capital raise, along with profit taking. Markets began the year strongly, before retreating on concerns for the banking sector following the collapse of Silicone Valley Bank and Credit Suisse. The **Dow Jones** rose **0.4%**, **NASDAQ 16.8%** and in the UK, the **FTSE** gained **2.4%**. Interest rate hikes were paused in April as investors now ponder if the next move in rates is down.



Newcrest Mining (NCM) up **32%** with a bid from Newmont Mining, which has since been increased in April, was the main highlight. The gold price hit record highs thanks to nervous markets.

PORTFOLIO HIGHLIGHTS

Leading performance drivers over the past 3 months

Code	Name	Movement (%)
Performance Contributors		
NCM	Newcrest Mining Ltd	32.7
EGY	Energy Technologies Ltd	16.33
Performance Detractors		
JRV	Jervois Global	-76.2
IOD	IODM Limited	-36.7

PORTFOLIO CHANGES

During the past 3 months the following changes were made to the portfolio

Stock Code	INCREASE		DECREASE		Held (%)
	Up (%)	Held (%)	Stock Code	Down (%)	
MXT	2.0	5.4			
GDI	5.0	10.0			
JRV	2.0	2.8			

STRATEGY UPDATE

The RBA continued to raise rates in the March quarter, however they've paused in April at 3.6%. Since May 2022 there has been a cumulative rise of 3.5%, or a 3,500% increase, no wonder mortgage stress is starting to hit households.

HOLDING UPDATES

Jervois Global (JRV)

Jervois Global (JRV) has come under severe selling pressure post a decision to suspend the final construction of the Idaho Cobalt Operation (ICO) until the cobalt market improves.

The market capitalisation has fallen to A\$137m (US\$92m). The current balance sheet position is US\$52m of cash, a US\$100m corporate bond and a US\$70m working capital debt facility drawn to US\$70m – so net debt of US\$118m. Jervois therefore has a current Enterprise Valuation of US\$210m (ignoring inventories of US\$113m which includes US\$70m of finished goods).

There are three main assets;

- The Kokkola cobalt refinery in Finland. Jervois bought this asset in 2021 for US\$200m. At the time we thought they had bought it cheap. In a normal mid-cycle cobalt market (US\$25/lb) – this asset should generate US\$40-50m EBITDA. Putting a 10x multiple on that would value Kokkola at ~US\$400-500m.
- The Idaho Cobalt Operation (ICO) in the US. Jervois has now spent US\$130m on this asset finishing off a previous US\$100m build of the asset by prior owners. So replacement cost is ~US\$230m.
- The SMP nickel/cobalt refinery in Brazil. The replacement value of this asset would be US\$250-300m. The asset is currently being brought back into production in 2024.

So the total asset value in Jervois is in the order of US\$870 – 1,030m. That is 4-5x higher than the current market valuation. The stock certainly looks cheap, but is not without risk.

The Kokkola refinery in Finland reported -ve EBITDA in the Dec quarter due to the fall in the cobalt price. A refinery operates by buying feed source at as low a price as possible, converting it to products (main costs are energy and labour) and then selling the final products at as high a price as possible. In a falling price environment, the lags in the system can mean refineries lose money – they are buying feedstock too high for the ultimate price they are selling the product at weeks later.

Once the cobalt price stabilises (it doesn't need to go up) – the refinery should return to profitability.

If the cobalt price starts to rise then the refinery will start to make very good earnings due to the reverse effect – buying cheap feedstock, and then selling it higher later.

Newcrest Mining (NCM)

Newcrest announced in early April an increased bid from Newmont Corporation. The bid has been increased to 0.40 Newmont shares for each Newcrest share held plus a US\$1.10ps fully franked dividend. At the last Newmont (NEM-USA) closing price of US\$51.09, this values Newcrest at ~A\$32.4ps, a 14.5% premium to its close on 14/4 of A\$28.28.

The gold price is moving higher on the back of a softening US\$, peaking interest rates and strong central bank buying. The sector is ripe for consolidation and equity market valuations of the ASX gold equities appear significantly below what corporates are prepared to pay in M&A transactions.

OUTLOOK

The three laggards of the last quarter have all improved since the end of March. We are still waiting on the market to recognise strong business performance in the small cap stocks. Kinatico (KYP), for example, is trading on less than 1x revenue and transitioning the business to predictable SaaS (software as a service) revenue. On top of this they are cash flow positive with M&A activity taking place across the sector.

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