

27 September 2021

Corp

Ticker GEM:AIM

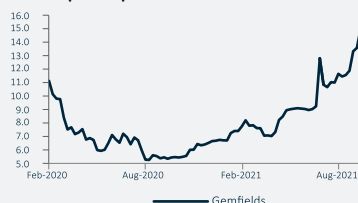
Mining
Shares in issue (m) 1,168.8
Next results FY Mar

Price 15.0p
Target price 25.0p
Upside 67%

Market cap £175.3m
Net debt/(cash) £21.0m
Other EV adjustments £0.0m
Enterprise value £196.3m

What's changed? From To
Adjusted EPS 0.9 2.4
Target price 19.0 25.0

Share price performance



| % | 1M | 3M | 12M |
|--------|------|------|-------|
| Actual | 30.4 | 69.0 | 160.9 |

Company description

The company mines for rubies in Mozambique and emeralds in Zambia.

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GEMFIELDS*

Strong interims and upgrade

Last week, Gemfields reported a very strong first half, with EBITDA OF \$43.5m and PAT of \$23.8m. This led to strong free cash generation (June net cash \$28.7m), which Gemfields should add to in the Q4 auctions and support growth capex and a potential dividend payment in FY22.

We have raised our FY21 revenue forecast from US\$161m to \$203m. Having previously been concerned that COVID would affect the second half auctions, the success of August's emerald auction, alongside strong outlook statements from the CEO and Chairman, changed our view. We now expect the two auctions planned for 4Q21 to be full size with strong pricing. Our FY21E revenue of \$203m produces EBITDA of US\$85m, PAT of \$37 and attributable PAT of \$29m.

YTD auctions have delivered strong volumes and pricing. Although this reflects pent-up demand, it also suggests established ruby and emerald markets that require Gemfields' products. To satisfy this demand, Gemfields will construct a 2nd wash plant (with associated yellow goods) at Montepuez in FY22 (we had assumed FY23). We adjusted our model to reflect, amongst other things, stronger pricing for commercial quality emeralds and reduced terrorism risk in Mozambique, adding \$55m to our NAV and taking Gemfields TP from 19p to 25p.

- **Dividend probable:** The Chairman's statement included "the board remains cautiously optimistic that it can deliver its long-held goal of distributing its maiden dividend to shareholders, hopefully during 2022" not quite a guarantee but read alongside bullish comments about the market, a dividend at some point during FY22 looks probable to us.
- **1H21 exceptional margin:** H1's strong cash generation was enhanced by lower than normal operating costs as both mines remained 'closed' in Q1 due to COVID. The mines ramped up during Q3 so opex will be higher in H2 and in future halves.
- **Balance sheet strength:** At the end of June, Gemfields had net cash of \$28.7m, consisting of \$67.3m cash and \$38.6m debt.
- **Strong outlook:** There remains a small chance that COVID travel restrictions delay or reduce the size of the two Q4 auctions; however, the new online sales process (where lots are viewed in multiple countries before a remote auction) vastly mitigates this risk. In the Interim Report, management made several bullish outlook statements about Q4 and beyond.
- **Target price increase:** We reduced Sedibelo's value to US\$25m, increased our emerald commercial quality price assumptions and reduced our Montepuez / Mozambique additional-risk discount from 20% to 10%. This adds US\$55m to our NAV and increases our share price target to 25p.

| Key estimates | | 2018A | 2019A | 2020A | 2021E | 2022E |
|---------------|-----|-------|-------|-------|-------|-------|
| Year end: | | Dec | Dec | Dec | Dec | Dec |
| Revenue | \$m | 206.1 | 216.2 | 34.6 | 203.1 | 231.3 |
| Adj EBITDA | \$m | 54.2 | 69.6 | -33.2 | 85.3 | 84.9 |
| Adj EBIT | \$m | 23.5 | 34.8 | -54.2 | 50.4 | 52.0 |
| Adj PBT | \$m | 14.7 | 30.3 | -60.0 | 55.4 | 50.1 |
| Adj EPS | c | -3.2 | 1.1 | -6.3 | 2.4 | 1.8 |
| DPS | c | 0.0 | 0.0 | 0.0 | 0.0 | 0.9 |

| Key valuation metrics | | 2018A | 2019A | 2020A | 2021E | 2022E |
|-----------------------|---|--------|-------|--------|-------|-------|
| EV/EBIT (adj) | x | 11.4 | 7.7 | -5.0 | 5.3 | 5.2 |
| P/E (adj) | x | -6.4 | 18.1 | -3.2 | 8.7 | 11.4 |
| Dividend yield | % | 0.0% | 0.0% | 0.0% | 0.0% | 4.2% |
| Free cash yield | % | -12.8% | 1.1% | -13.3% | 20.9% | 11.5% |
| Pre-tax ROCE | % | 3.9% | 5.5% | -10.0% | 9.1% | 9.3% |

Strong interims and upgrade

| Income statement | | 2019A | 2020A | 2021E | 2022E |
|--------------------------------------|------------|-------------|--------------|-------------|-------------|
| Year end: | | Dec | Dec | Dec | Dec |
| Sales | \$m | 216.2 | 34.6 | 203.1 | 231.3 |
| Gross profit | \$m | 91.6 | -24.5 | 92.8 | 103.5 |
| EBITDA (adjusted) | \$m | 69.6 | -33.2 | 85.3 | 84.9 |
| EBIT (adjusted) | \$m | 34.8 | -54.2 | 50.4 | 52.0 |
| Associates/other | \$m | 0.0 | 0.0 | 7.8 | 0.0 |
| Net interest | \$m | -4.5 | -5.8 | -2.8 | -1.8 |
| PBT (adjusted) | \$m | 30.3 | -60.0 | 55.4 | 50.1 |
| Total adjustments | \$m | 37.1 | -39.2 | 0.0 | 0.0 |
| PBT (stated) | \$m | 67.4 | -99.2 | 55.4 | 50.1 |
| Tax charge | \$m | -28.2 | 6.0 | -18.5 | -19.0 |
| Minorities/Disc ops | \$m | 10.8 | -7.9 | 8.4 | 9.3 |
| Reported earnings | \$m | 28.4 | -85.3 | 28.6 | 21.8 |
| Adjusted earnings | \$m | 13.3 | -73.8 | 28.6 | 21.8 |
| Shares in issue (year end) | m | 1,171.0 | 1,168.8 | 1,168.8 | 1,168.8 |
| EPS (stated) | c | 2.2 | -7.3 | 2.4 | 1.9 |
| EPS (adjusted, fully diluted) | c | 1.1 | -6.3 | 2.4 | 1.8 |
| DPS | c | 0.0 | 0.0 | 0.0 | 0.9 |

| Cash flow | | 2019A | 2020A | 2021E | 2022E |
|--------------------------------------|------------|-------------|--------------|-------------|-------------|
| Year end: | | Dec | Dec | Dec | Dec |
| EBITDA | \$m | 67.4 | -33.2 | 85.3 | 84.9 |
| Net change in working capital | \$m | -25.3 | 31.3 | -16.6 | 5.5 |
| Other operating items | \$m | 4.3 | -3.3 | 2.2 | 0.0 |
| Cash flow from op. activities | \$m | 46.4 | -5.2 | 70.9 | 90.3 |
| Cash interest | \$m | -3.3 | -3.0 | -1.7 | -0.3 |
| Cash tax | \$m | -9.7 | -15.0 | -10.4 | -19.0 |
| Capex | \$m | -30.8 | -8.6 | -8.8 | -43.5 |
| Other items | \$m | | | | |
| Free cash flow | \$m | 2.5 | -31.8 | 50.0 | 27.6 |
| Acquisitions / disposals | \$m | 35.2 | 0.0 | 0.0 | 0.0 |
| Dividends | \$m | 0.0 | 0.0 | 0.0 | -10.0 |
| Shares issued | \$m | -14.4 | -0.2 | 0.0 | 0.0 |
| Other | \$m | -7.8 | -6.0 | -4.0 | -1.3 |
| Net change in cash flow | \$m | 15.6 | -38.0 | 46.0 | 16.2 |
| Opening net cash (debt) | \$m | 9.8 | 25.4 | -12.6 | 32.2 |
| Closing net cash (debt) | \$m | 25.4 | -12.6 | 32.2 | 46.9 |

| Balance sheet | | 2019A | 2020A | 2021E | 2022E |
|------------------------------|------------|--------------|--------------|--------------|--------------|
| Year end: | | Dec | Dec | Dec | Dec |
| Tangible fixed assets | \$m | 376.9 | 362.7 | 337.0 | 346.6 |
| Goodwill & other intangibles | \$m | 55.2 | 51.5 | 53.3 | 54.3 |
| Other non current assets | \$m | 75.3 | 43.7 | 51.5 | 51.5 |
| Net working capital | \$m | 168.7 | 133.3 | 141.9 | 136.4 |
| Other assets | \$m | 0.0 | 0.0 | 0.0 | 0.0 |
| Other liabilities | \$m | -122.5 | -95.6 | -95.6 | -95.6 |
| Gross cash & cash equivs | \$m | 78.2 | 43.9 | 67.0 | 68.5 |
| Capital employed | \$m | 631.8 | 539.5 | 555.0 | 561.7 |
| Gross debt | \$m | 52.8 | 56.5 | 35.1 | 22.0 |
| Net pension liability | \$m | 0.0 | 0.0 | 0.0 | 0.0 |
| Shareholders equity | \$m | 494.3 | 412.6 | 441.1 | 452.9 |
| Minorities | \$m | 84.7 | 70.4 | 78.8 | 86.8 |
| Capital employed | \$m | 631.8 | 539.5 | 555.0 | 561.7 |

| Growth analysis | | 2019A | 2020A | 2021E | 2022E |
|-----------------|---|--------|---------|--------|--------|
| Year end: | | Dec | Dec | Dec | Dec |
| Sales growth | % | 4.9% | -84.0% | 487.4% | 13.9% |
| EBITDA growth | % | 28.5% | -147.7% | 357.1% | -0.5% |
| EBIT growth | % | 47.7% | -255.9% | 193.0% | 3.1% |
| PBT growth | % | 106.2% | -298.0% | 192.3% | -9.5% |
| EPS growth | % | 135.2% | -656.7% | 137.3% | -23.6% |
| DPS growth | % | n/m | n/m | n/m | n/m |

| Profitability analysis | | 2019A | 2020A | 2021E | 2022E |
|------------------------|---|-------|---------|-------|-------|
| Year end: | | Dec | Dec | Dec | Dec |
| Gross margin | % | 42.3% | -70.9% | 45.7% | 44.8% |
| EBITDA margin | % | 32.2% | -96.0% | 42.0% | 36.7% |
| EBIT margin | % | 16.1% | -156.8% | 24.8% | 22.5% |
| PBT margin | % | 14.0% | -173.6% | 27.3% | 21.7% |
| Net margin | % | 6.1% | -213.4% | 14.1% | 9.4% |

| Cash flow analysis | | 2019A | 2020A | 2021E | 2022E |
|-----------------------------------|-----|--------|-------|-------|--------|
| Year end: | | Dec | Dec | Dec | Dec |
| Cash conv'n (op cash / EBITDA) | % | 68.8% | n/m | 83.1% | 106.5% |
| Cash conv'n (FCF / EBITDA) | % | 3.8% | 96.0% | 58.6% | 32.5% |
| U/lying FCF (capex = depn) | \$m | -1.4 | -44.2 | 23.9 | 38.2 |
| Cash quality (u/l FCF / adj earn) | % | -10.8% | 59.9% | 83.7% | 174.9% |
| Investment rate (capex / depn) | x | 0.9 | 0.4 | 0.3 | 1.3 |
| Interest cash cover | x | 14.1 | n/a | 42.3 | 306.3 |
| Dividend cash cover | x | n/m | n/a | n/m | 2.8 |

| Working capital analysis | | 2019A | 2020A | 2021E | 2022E |
|-----------------------------|------|-------|--------|-------|-------|
| Year end: | | Dec | Dec | Dec | Dec |
| Net working capital / sales | % | 78.0% | 385.8% | 69.9% | 59.0% |
| Net working capital / sales | days | 285 | 1,408 | 255 | 215 |
| Inventory (days) | days | 187 | 1,244 | 194 | 177 |
| Receivables (days) | days | 148 | 392 | 128 | 101 |
| Payables (days) | days | 50 | 228 | 67 | 63 |

| Leverage analysis | | 2019A | 2020A | 2021E | 2022E |
|--------------------------------|---|----------|-------|----------|----------|
| Year end: | | Dec | Dec | Dec | Dec |
| Net debt / equity | % | net cash | 3.1% | net cash | net cash |
| Net debt / EBITDA | x | net cash | n/a | net cash | net cash |
| Liabilities / capital employed | % | 8.4% | 10.5% | 6.3% | 3.9% |

| Capital efficiency & intrinsic value | | 2019A | 2020A | 2021E | 2022E |
|--------------------------------------|---|-------|--------|-------|-------|
| Year end: | | Dec | Dec | Dec | Dec |
| Adjusted return on equity | % | 2.7% | -17.9% | 6.5% | 4.8% |
| RoCE (EBIT basis, pre-tax) | % | 5.5% | -10.0% | 9.1% | 9.3% |
| RoCE (u/lying FCF basis) | % | -0.2% | -8.2% | 4.3% | 6.8% |
| NAV per share | c | 42.2 | 35.3 | 37.7 | 38.8 |
| NTA per share | c | 37.5 | 30.9 | 33.2 | 34.1 |

FY21E upgrade

Based on management's bullish comments in last week's interims, we have upgraded our numbers. Tax and government royalties also increase, however much of the additional revenue hits the bottom line. US\$29m of net profit equates to EPS of 2.4p.

Note that Profit After Tax includes circa US\$30m of depreciation charges so a better metric for profitability is free cashflow before financing.

Figure 1: Changes to FY21 forecast

| | Previous US\$ | New US\$ |
|------------------------------------|------------------|-------------|
| Revenue | 161.98 | 203.06 |
| EBITDA | 53.05 | 85.32 |
| PBT | 22.52 | 55.39 |
| PAT | 17.57 | 36.93 |
| PAT (attributable to shareholders) | 11.25 | 28.57 |
| FCF | -8.14 | 48.33 |
| Net debt | 24.11 | 31.84 |

Source: finnCap

Strong interims and upgrade

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