

# Gemfields Group

Auction results

## Maxi-mini auction results

As travel restrictions prevented customers travelling to auctions, Gemfields turned to a series of mini-auctions to sell rough rubies and emeralds. These generated US\$58.9m from ruby sales and US\$31.4m from emeralds this year making the 'mini' in mini-auctions appear misplaced. Not only does the US\$90.3m in sales shore up the balance sheet, but the prices achieved point to strong customer demand for Gemfields' stones.

Year end	Revenue (\$m)	PBT* (\$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/19	216.2	55.9	1.3	0.0	8.8	N/A
12/20	34.6	(84.7)	(6.1)	0.0	N/A	N/A
12/21e	190.1	1.2	(1.5)	0.0	N/A	N/A
12/22e	240.3	52.2	1.5	0.0	7.7	N/A

Note: \*PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

## Mini-auctions generated US\$90.3m in revenue

Gemfields has announced results from five high-quality emerald and seven ruby mini-auctions in March/April 2021. The emerald mini auctions generated US\$31.4m in sales, the highest since March 2016, and the ruby mini-auctions US\$58.9m (even though one large lot of lower quality rubies remained unsold). Prices were strong, with emeralds at an all-time record of US\$115.59/ct (partly because of the mix offered). The US\$90.3m from the mini auctions addresses the risk that Gemfields could need to raise further capital to weather the COVID-19 storm. Gemfields ended 2020 with cash of US\$43.9m (net debt of US\$12.6m). With the auction proceeds this should provide ample funding headroom to ramp up at Kagem and Montepuez Ruby Mining (MRM) and through to the next planned auctions in late 2021. We expect cash to remain above US\$29m through the year with a further US\$10m available in undrawn facilities.

## 2020 results reflect a difficult year

Gemfields' full year 2020 results cover a period during which both the Kagem and MRM mines were suspended from March/April and where normal auctions could not be held after February. Group revenue fell by 84% to US\$34.6m and EBITDA fell to a loss of US\$30.0m in 2020 against an EBITDA profit of US\$80.9m in 2019.

## Valuation: Sum of the parts of US\$345m or 22p/share

We value Gemfields on a discounted cash flow sum-of-the-parts at a 10% discount rate. Our updated valuation is US\$345m (22p or ZAR4.21 per share) compared to a previous valuation of US\$320m (21p or ZAR4.14 per share). With forecasts not significantly changed, the key valuation change results from the rolling forward of the valuation date (and net cash balance) to 31 December 2020 resulting in a slight value uplift as positive future cash flows are discounted by one less year.

## Metals & mining

29 April 2021

Price **ZAR1.65**

Market cap **ZAR1,929**

ZAR14.28/US\$

Net debt (US\$m) at 31 December 2020 12.6

Shares in issue 1,168.8m

Free float 72%

Code GML/GEM

Primary exchange Johannesburg

Secondary exchange AIM

## Share price performance



% 1m 3m 12m

Abs 23.5 5.0 6.3

Rel (local) 22.2 (2.4) (22.1)

52-week high/low ZAR1.75 ZAR1.10

## Business description

Gemfields Group is a world-leading supplier of responsibly sourced coloured gemstones. It owns 75% of Montepuez Ruby Mining in Mozambique, 75% of Kagem Mining in Zambia, the Fabergé jewellery business and an investment in Sedibelo Platinum.

## Next events

Half year results September 2021

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## Mini-auctions generated US\$90.3m in total revenue

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Gemfields' March and April 2021 ruby and emerald mini-auctions generated sales of US\$90.3m – a very positive result not only considering the limitations of the alternative process but also in absolute terms. Pricing at both auctions was very strong, albeit impacted by the mix of stones sold. The success of the mini auctions shores up the Gemfields' balance sheet and points to very solid market demand for Gemfields high quality ruby and emerald production from MRM and Kagem.

### Ruby mini-auction sales of US\$58.9m

Between 15 March and 8 April Gemfields held a series of seven ruby mini-auctions consisting of mixed quality-rubies mined at MRM prior to suspension of operations there in April 2020. Stones were made available for viewing in Bangkok, Dubai and Jaipur and then auctions took place via an online platform.

The ruby mini-auctions generated:

- **US\$58.9m in total sales (versus average US\$62.15m for last four pre-COVID-19 auctions).**
- **Exceptional pricing of US\$171.33 per carat (affected by mix):** While average pricing achieved at the ruby mini-auctions is not representative of the usual MRM mixed-quality product mix (because one very large lot of lower quality stones did not achieved the reserve price and remained unsold) it is still good news and Gemfields said that it was 'very encouraged by the strong appetite from our clients and by the prices realised.'

Production has resumed at MRM and is expected to ramp up to full capacity by the end of April. The company hopes that the next mixed-quality auction will take place late this year.

MRM is located 280km from the town of Palma (the location of recent insurgent attacks) in Mozambique. While not affected by the conflict directly, Gemfields is closely monitoring the situation and working with the government to provide humanitarian relief for the many thousands of displaced people.

### Emerald mini-auction sales of US\$31.4m

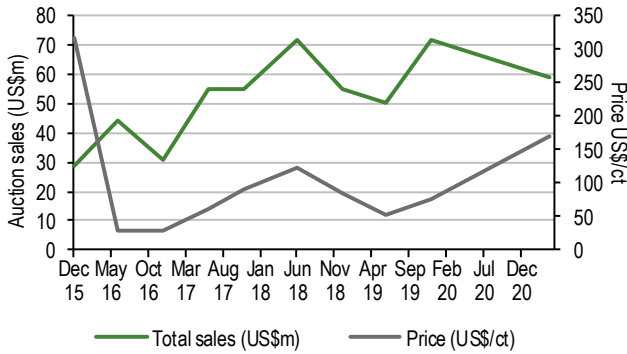
Between 15 March and 17 April five emerald mini-auctions were held of high-quality emeralds mined at Kagem prior to suspension of operations there in March 2020. Stones were made available for viewing in Tel Aviv, Dubai and Jaipur followed by auctions via an online platform.

The emerald mini auctions achieved:

- **US\$31.4m in total sales – the highest emerald auction figure since March 2016.**
- **Average price of US\$115.59/ct,** partly reflects mix but even adding the November/December mini auction to give a more representative average for all the mini auctions to date of US\$93.2/ct, this would still be an all-time high.
- **59 companies placed bids (and on average 18 bids were received per lot, a new high)**

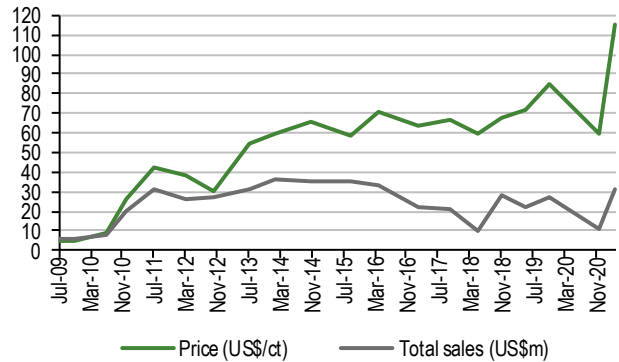
Production has resumed at Kagem and is expected to ramp up to full capacity by the end of April.

**Exhibit 1: Ruby auction results (total sales and price per carat)**



Source: Gemfields

**Exhibit 2: High-quality emerald auction results (total sales and price per carat)**



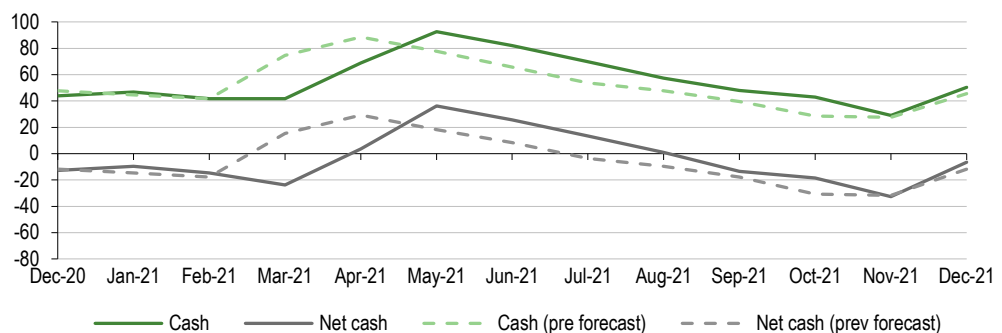
Source: Gemfields

## Strong auction results address balance sheet risk

In our December 2020 [note](#) we calculated that Gemfields should not need to raise additional capital provided that full emerald and ruby auctions could be held in March 2021 or soon thereafter. Despite not being able to hold full in-person auctions at all in H1, the mini-auction results have exceeded the US\$70-80m figure that we had expected for full in person auctions with total auction proceeds of US\$90.3m. We have increased our group full year revenue forecast to US\$190.1m (from US\$183.5m previously) to capture this strong auction result, partially offset by slightly lower inventory than available for sale in H2.

Operations at both Kagem and MRM resumed in March ramping up to full production by the end of April. That will increase Gemfields' monthly cost base to around US\$12m a month (from US\$5m a month when these operations were on care and maintenance). Nevertheless, buffered with cash from the mini-auctions, Gemfields now has sufficient cash reserves to take the company comfortably through to the next planned auctions in late Q4. The chart below shows our updated forecast cash and net cash balances on a monthly basis. We now expect Gemfields to end 2021 with cash of US\$50.4m and net debt of US\$6.6m (from net debt of US\$11.0m forecast previously).

**Exhibit 3: Monthly cash and net cash forecasts (US\$m)**



Source: Edison Investment Research

The company continues to expect to return to its standard auction process in H2 (with auctions held fully in person in a single location to which customers travel), however the success of the recent mini-auctions means there is a clear fallback process if restrictions persist.

At 31 December 2020, Gemfields had cash of US\$43.9m, and US\$56.5m in borrowings comprising:

- US\$18m at Kagem under a (fully drawn) ABSA Zambia term loan which runs to 2024 with US\$4.5m repayable in December 2021;
- US\$10m at Kagem under a (fully drawn) ABSA Zambia revolver (renewable 2022); and
- US\$28.5m at MRM under ABSA Mozambique and BCI overdraft facilities (renewable annually) totalling US\$30m.

At December 2020 all facilities were close to fully drawn. In March 2021 BCI granted MRM a further US\$8.9m facility to be repaid from the next auction proceeds (or within six months). On repayment, MRM will, with agreement from BCI, have access to a US\$15m facility repayable over four years.

Where earlier this year there was a very real risk that Gemfields would need to look for additional funding to take it through this COVID-19 period, we believe that investors can now appraise the longer-term value proposition without concerns around nearer-term funding risk.

## 2020 results reflected a very tough year

The impact of COVID-19 saw operations at Gemfields' Kagem emerald mine in Zambia suspended in March 2020 followed by operations at the MRM ruby mine in Mozambique in April 2020. Operations remained suspended through the rest of the year and have only resumed in recent weeks at both operations. Perhaps more concerning for the company and investors, Gemfields was only able to hold one regular-format commercial quality emerald auction in February 2020 generating US\$11.4m and thereafter was unable to hold regular auctions because customers were unable to travel internationally. In November and December, Gemfields held its emerald mini-auctions generating US\$10.9 meaning that for the whole of 2020 the company generated just US\$22.3m in auction revenues against US\$200.5m in 2019. Fabergé was also not immune from the impact of COVID-19 with a number of outlets closed during the early stage of the pandemic and sales falling to US\$7.1m from US\$10.5m in 2019. Group revenue totalled US\$34.6m, down 84% year-on-year.

The company cut costs dramatically in response, with total cash mining and production costs reduced from US\$63.4 in 2019 to US\$37.7m in 2020, and SG&A falling from US\$51.7m in 2019 to US\$27.8m in 2020. Nevertheless, Gemfields saw a 2020 EBITDA loss of US\$30.0m in 2020 against an EBITDA profit of US\$80.9m in 2019.

Gemfields' 2020 results also reflect write-downs of US\$13.5m relating mainly to Fabergé intangible assets and inventory. The group also took a US\$27.9m fair value loss on its 6.54% stake in Sedibelo. The stake in Sedibelo is non-core for Gemfields and it has engaged advisors to look for buyers for this holding, but the indirect holding structure (through a 23.65% equity holding in a Luxembourg holding company, Pallinghurst Ivy Lane Capital) complicates the investment proposition for potential purchasers. The management of Pallinghurst Ivy Lane Capital has indicated its intention to unbundle the holding, which could benefit the sale process.

Gemfields reported a 2020 loss before tax of US\$99.2m (2019 PBT of US\$67.4m) and loss per share of US\$0.07 (2019 EPS of US\$0.02).

### Exhibit 4: 2020 results key metrics

	2019	2020
Revenue (US\$m)	216.2	34.6
EBITDA (US\$m)	80.9	(30.0)
PBT* (US\$m)	67.4	(99.2)
EPS* (US\$/share)	0.02	(0.07)
Net cash (debt)	25.4	(12.6)

Source: Gemfields. Note: \*As reported, before adjustment for write-downs, share based payments and amortisation of intangibles.

## Updated financial forecasts reflect only minor changes

As the months of continued COVID-19 travel restrictions continued, earlier this year we had begun to fear that our 2021 forecasts for Gemfields may prove optimistic if the company could not hold auctions in H1. However, the success of the mini-auctions has put those fears to rest and our 2021 forecasts reflect only relatively minor changes compared to our previous forecasts including a US\$7m increase in forecast revenue following the strong mini-auction results.

We now forecast 2021 EBITDA of US\$33m (previously US\$29m), PBT of US\$1m (US\$2m previously with the difference explained by higher forecast depreciation)) and closing net debt of US\$6.6m (previously US\$11.0m net debt).

### Exhibit 5: Forecast key metrics

	Previous	New
Group revenue 2021 (US\$m)	183	190
Group EBITDA 2021(US\$m)	29	33
PBT 2021 (US\$m)	2	1
EPS 2021 (c)	(1.6)	(1.5)
<b>Closing net cash (debt) 2021 (US\$m)</b>	<b>(11.0)</b>	<b>(6.6)</b>
Group revenue 2022 (US\$m)	243	240
Group EBITDA 2022 (US\$m)	84	81
PBT 2022 (US\$m)	58	52
EPS 2022 (c)	1.7	1.5
<b>Closing net cash (debt) 2022 (US\$m)</b>	<b>(1.6)</b>	<b>7.9</b>

Source: Edison Investment Research

## Sensitivities

In addition to the normal operational, safety, environmental and other risks of any mining operation, Gemfields has two key risks currently that we think investors should pay particular attention to, being heightened political and security risks in Mozambique and coloured gemstone market risk.

### Heightened political and security risk in Mozambique

Since 2017, there has been a rise in insurgent attacks in the Cabo Delgado region in northern Mozambique, where Gemfields' MRM mine is located. The insurgents are linked to Islamist militant groups with connections to Islamic State but are also tapping into local political grievances. Those attacks escalated through 2020 and it is estimated that some 700,000 civilians have been displaced by the violence. While the Montepuez region itself has been less affected and Gemfields operations have not been directly affected, the growing security crisis in this region is a key risk for Gemfields.

### Coloured gemstone market risk

While the success of the March/April mini-auctions indicated a strong market for coloured gemstones, the strength of those results reflected in part pent-up demand as no ruby auctions were held by MRM at all in 2020, while Kagem sold just US\$10.9m in high-quality emeralds (and US\$11.4m in commercial-quality emeralds in February 2020). Whether coloured gemstone market demand will remain strong, particularly given continued COVID-19 risks in India, which is a key emerald cutting and polishing market, remains a key risk for the company.

## Valuation

As previously, we value Gemfields on a discounted cash flow sum-of-the-parts basis (at a 10% discount rate). Our updated valuation reflects a valuation date and net cash balance as at 31 December 2020 (previously 31 December 2019).

With our forecasts little changed, the key change to our valuation reflects this rolling forward of the valuation base date.

- Our updated sum-of-the-parts valuation totals US\$345m or 22p per share (previously US\$320m or 21p per share).
- The rand per-share valuation (of interest mostly to South African investors) is negatively affected by the impact of the stronger rand (ZAR14.28/US\$ vs ZAR15.12/US\$ previously) on the translation of our US dollar-driven valuation of Gemfields to rand per share.
- We value Gemfields' share in Sedibelo on a resource multiple of US\$10/oz applied to Sedibelo's 87Moz PGM resource but with a 30% discount to reflect Gemfields' minority stake. Following the 2020 fair value adjustment, our US\$40m valuation is above the company's US\$29.6m balance sheet valuation, which we think is justified given the further rise in PGM prices since the 31 December 2020 date of the company's valuation.

### Exhibit 6: Sum-of-the-parts valuation

	New valuation	Previous
Kagem (75%) US\$m	171	170
Montepuez (75%) US\$m	295	249
Fabergé (100%) US\$m	21	13
Sedibelo (6.54%) US\$m	40	40
Corporate overheads US\$m	(169)	(176)
Net cash US\$m (31 December 2019)	(13)	25
<b>Sum of the parts valuation US\$m</b>	<b>345</b>	<b>320</b>
Rand per share	4.21	4.14
Pence per share	22	21

Source: Edison Investment Research

**Exhibit 7: Financial summary**

	US\$m	2018	2019	2020	2021e	2022e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS
<b>INCOME STATEMENT</b>						
Revenue		206.1	216.2	34.6	190.1	240.3
Cost of Sales		(123.5)	(118.5)	(58.0)	(128.7)	(121.7)
Gross Profit		82.5	97.8	(23.4)	61.4	118.5
EBITDA		58.9	80.9	(30.0)	33.1	80.8
Operating Profit (before amort. and except.)		28.2	46.1	(51.1)	5.5	54.9
Fair value gains (losses)		(41.9)	14.3	(27.9)	0.0	0.0
Exceptionals		(22.6)	13.2	(13.5)	0.0	0.0
Share-based payments		(4.2)	(1.7)	(0.9)	(1.5)	(2.0)
Reported operating profit		(40.4)	71.9	(93.4)	4.0	52.9
Net Interest		(8.8)	(4.5)	(5.8)	(4.3)	(2.8)
Joint ventures & associates (post tax)		0.0	0.0	0.0	0.0	0.0
Profit Before Tax (norm)		(22.5)	55.9	(84.7)	1.2	52.2
Profit Before Tax (reported)		(53.9)	67.4	(99.2)	(0.3)	50.2
Reported tax		(6.5)	(28.2)	6.0	(14.1)	(25.1)
Profit After Tax (norm)		(29.0)	27.6	(78.8)	(12.9)	27.0
Profit After Tax (reported)		(60.4)	39.1	(93.2)	(14.4)	25.0
Minority interests		(1.8)	(10.8)	7.9	(5.2)	(9.1)
Net income (normalised)		(30.8)	16.9	(70.8)	(18.1)	17.9
Net income (reported)		(62.2)	28.4	(85.3)	(19.6)	15.9
Avg No of Shares Outstanding (m)		1,170	1,265	1,169	1,169	1,169
EPS - basic normalised (c)		(2.6)	1.3	(6.1)	(1.5)	1.5
EPS - normalised (c)		(2.6)	1.3	(6.1)	(1.5)	1.5
EPS - basic reported (c)		(5.3)	2.2	(7.3)	(1.7)	1.4
Dividend per share (c)		0.0	0.0	0.0	0.0	0.0
Revenue growth (%)		152.4	4.9	(-84.0)	449.9	26.4
Gross Margin (%)		40.1	45.2	-67.8	32.3	49.3
EBITDA Margin (%)		28.6	37.4	-86.9	17.4	33.6
Normalised Operating Margin (%)		13.7	21.3	-147.7	2.9	22.9
<b>BALANCE SHEET</b>						
Fixed Assets		509.7	507.4	457.9	452.4	458.3
Intangible Assets		52.3	55.2	51.5	51.5	51.5
Tangible Assets		365.0	376.9	362.7	360.0	367.9
Investments & other		92.4	75.3	43.7	40.9	38.9
Current Assets		224.4	276.8	198.8	203.1	207.3
Stocks		99.2	110.7	117.8	94.7	90.8
Debtors		62.1	87.8	37.1	58.0	62.5
Cash & cash equivalents		63.0	78.2	43.9	50.4	53.9
Other		0.0	0.0	0.0	0.0	0.0
Current Liabilities		(60.6)	(75.2)	(59.5)	(78.3)	(76.1)
Creditors		(28.2)	(29.9)	(18.2)	(25.0)	(27.0)
Tax payable		(1.4)	(16.3)	(4.3)	(11.3)	(10.1)
Short term borrowings		(23.2)	(24.8)	(33.0)	(38.0)	(35.0)
Other		(7.9)	(4.2)	(4.0)	(4.0)	(4.0)
Long Term Liabilities		(123.4)	(130.1)	(114.2)	(109.7)	(101.7)
Long term borrowings		(30.0)	(28.0)	(23.5)	(19.0)	(11.0)
Other long term liabilities		(93.4)	(102.1)	(90.7)	(90.7)	(90.7)
Net Assets		550.1	578.9	483.0	467.5	487.8
Minority interests		(73.9)	(84.7)	(70.4)	(73.0)	(75.4)
Shareholders' equity		476.2	494.3	412.6	394.5	412.4
<b>CASH FLOW</b>						
Op Cash Flow before WC and tax		58.9	80.9	(30.0)	33.1	80.8
Working capital		(29.7)	(25.7)	25.5	16.0	0.1
Exceptional & other		0.3	(8.8)	(0.6)	0.0	0.0
Tax		(24.4)	(9.7)	(15.0)	(11.3)	(23.1)
Net operating cash flow		5.1	36.7	(20.166)	37.8	57.8
Capex		(29.0)	(30.8)	(8.6)	(24.8)	(33.8)
Acquisitions/disposals		77.4	35.2	0.1	0.0	0.0
Net interest		(4.4)	(3.3)	(4.1)	(4.3)	(2.8)
Equity financing		(4.7)	(14.4)	(0.2)	0.0	0.0
Dividends		(5.9)	0.0	0.0	(2.6)	(6.7)
Other		(2.9)	(7.8)	(5.0)	0.0	0.0
Net Cash Flow		35.6	15.6	(38.123)	6.1	14.5
Opening net debt/(cash)		25.7	(9.8)	(25.4)	12.6	6.6
FX		(0.1)	0.0	0.1	0.0	0.0
Other non-cash movements		0.0	0.0	0.0	0.0	0.0
Closing net debt/(cash)		(9.8)	(25.4)	12.6	6.6	(7.9)

Source: Gemfields accounts, Edison Investment Research

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