A new JSE listing - Thungela

Perspectives: June 9th, 2021

New stock exchange listings are not made equal -there are many different kinds. Some great, some not so great. We start our analysis by trying to figure out ***why*** a business is listing. We are looking to first understand its origin story and context. It helps us to also pose questions such as *who* the primary beneficiaries of the listing process are. If for whatever reason it is *not* likely to be the new shareholders, we propose being careful.

Thungela made its debut on the JSE earlier this week, which in and of itself looked out of place, as there has been net delistings from our local exchange for several years now.

Thungela is a new name for an old company, first established in 1945. In isiZulu Thungela means 'to ignite'. With over ZAR18bn in annual sales and over 7,500 people, it is a significant producer of thermal coal, primarily for export. It also owns meaningful ownership stakes in a coal processing plant and the Richards Bay Coal Terminal.

Thermal coal is mainly used by power stations, who burn it to create the steam that generates electricity. Burning it produces greenhouse gases that cause global warming. So, it is nasty stuff by most people's standards, and especially by today's global ESG standards.

Thungela listed on the JSE by way of *unbundling* from its former owner - Anglo American. This is also called a 'spin-off'. We make a point of taking a good look at all spin-offs, because they can present sensible investment opportunities.

Thungela ticks a few of our boxes - it is an established, scale business, it is unloved (seriously, it is a *South African* *coal* producer?), its small market cap means it is highly unlikely to ever be included in key benchmark indices, and there are readily identifiable owners that are almost certain to be forced sellers. So far so good.

Unfortunately, it also lit up many of our red flags. The executives do not own any shares, thermal coal prices are well above long-term averages, their proven life-of-mine is only 8 years (in the capital-intensive global mining industry this amount of time is a blink), they are loss-making, they have significant net debt on the balance sheet, and they also have unquantifiable off-balance sheet environmental rehabilitation contingent liabilities [*this basically means they do not yet know how much it will cost them to properly clean up what they have done to Mother Nature*].

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*"Proposed revised financial provisions regulations (the 2019 Financial Provisioning regulations) are set to **significantly** increase the quantum of financial provisioning required to be held by companies, including the Group, in relation to their environmental liability, closure and decommissioning obligations. If such proposed regulations come into force as currently drafted, the Group is likely to have to **significantly** increase its financial provisioning and the level of guarantees required to be held for closure liabilities in order to comply"*

Source: Thungela Prospectus, page 130. Emphasis added.

Our work continues...

Daniel Malan
Managing Director & Chief Investment Officer
daniel@perspectiveim.co.za

Perspective Investment Management
www.perspectiveim.co.za