

1 January 2022

Corp

Ticker	GEM:AIM
Mining	
Shares in issue (m)	1,169.5
Next results	FY Mar

Price	13.3p
Target price	25.0p
Upside	89%

Market cap	£155.0m
Net debt/(cash)	-£21.3m
Other EV adjustments	£52.4m
Enterprise value	£185.9m

What's changed?	From	To
Adjusted EPS	4.3	n/c
Target price	25.0	n/c

Share price performance



%	1M	3M	12M
Actual	0.0	-11.1	96.3

Company description

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

Charlie Long

Research Analyst
clong@finncap.com
020 3772 4683

Sales desk 020 7220 0522

Trading desk 020 7220 0533

* denotes corporate client of finnCap

GEMFIELDS*

Maiden dividend expected in 1Q21

2021 was a significant year in Gemfields history. Record revenues of >US\$250m (16% above the previous FY19 record) reflected (1) pent-up demand created by COVID, but more importantly (2) strong underlying ruby and emerald demand from a developed customer base.

Developing the customer base has been a gradual 10-year process, whereby Gemfields has built its reputation as a consistent, long-term supplier. This allowed the downstream players to invest with confidence in the design, manufacture, promotion and retailing of new ruby and emerald jewellery ranges. The market is now well developed, which should ensure demand is sustained.

Given Gemfields' customer base and net cash balance sheet, it is likely to declare a maiden dividend in 1Q22. It also has plans to increase sales (FY23 onwards) by expanding production capacity at the ruby mine (Montepuez). Together, this creates a strong investment case, while the dividend will differentiate Gemfields from much of the small cap mining sector.

- **What are the underlying industry dynamics?** Gemfields produces c.60% of global emerald supply and 35% of ruby supply. Historical and future demand growth is driven by Gemfields' ability to supply large volumes of rough gems to a consistent standard over the long term.
- Commenting on December's record ruby auction, Gemfields' M&D of Marketing & Sales Adrian Banks stated: "This has been the strongest ruby auction in Gemfields' history and we're very pleased with the trajectory and growth of the downstream ruby sector. Professionalised and dependable supply has always been the key to unlocking growth".
- **Why is Gemfields going to perform well in 2022?** The main catalyst for GEM in FY22 is our expectation of a maiden dividend, likely to be declared at the FY21 results in March. Its FY21 financial results could also create some interest in the shares – we forecast FY21 EBITDA of US\$123m.
- **Why do we think the shares are cheap?** FY21 EBITDA and EPS will be extraordinary due to lower-than-normal operating costs (cost cutting implemented due to COVID-19). Based on the more representative FY22E EBITDA of US\$102m, Gemfields is trading on 2.4x EV/EBITDA and an FY22E P/E of 5.9x.
- **Where could we be wrong?** As a mining company operating in Southern Africa, Gemfields is exposed to a range of uncontrollable risks. These include unforeseen changes to tax regime and potential security issues. There are also risks in the mines themselves, such as geological risk, where the grade of the ore may change unexpectedly.

Key estimates		2018A	2019A	2020A	2021E	2022E
Year end:		Dec	Dec	Dec	Dec	Dec
Revenue	\$m	206.1	216.2	34.6	251.7	251.3
Adj EBITDA	\$m	54.2	69.6	-33.2	123.0	101.6
Adj EBIT	\$m	23.5	34.8	-54.2	97.5	70.1
Adj PBT	\$m	14.7	30.3	-60.0	102.5	68.7
Adj EPS	c	-3.2	1.1	-6.3	4.3	2.3
DPS	c	0.0	0.0	0.0	0.0	0.9

Key valuation metrics		2018A	2019A	2020A	2021E	2022E
EV/EBIT (adj)	x	10.6	7.2	-4.6	2.6	3.6
P/E (adj)	x	-5.5	15.7	-2.8	4.1	7.7
Dividend yield	%	0.0%	0.0%	0.0%	0.0%	4.8%
Free cash yield	%	-14.7%	1.2%	-15.3%	28.6%	12.4%
Pre-tax ROCE	%	3.9%	5.5%	-10.0%	16.7%	12.0%

Investment ideas for 2022

Income statement		2019A	2020A	2021E	2022E
Year end:		Dec	Dec	Dec	Dec
Sales	\$m	216.2	34.6	251.7	251.3
Gross profit	\$m	91.6	-24.5	138.5	122.7
EBITDA (adjusted)	\$m	69.6	-33.2	123.0	101.6
EBIT (adjusted)	\$m	34.8	-54.2	97.5	70.1
Associates/other	\$m	0.0	0.0	7.8	0.0
Net interest	\$m	-4.5	-5.8	-2.8	-1.5
PBT (adjusted)	\$m	30.3	-60.0	102.5	68.7
Total adjustments	\$m	37.1	-39.2	0.0	0.0
PBT (stated)	\$m	67.4	-99.2	102.5	68.7
Tax charge	\$m	-28.2	6.0	-37.4	-29.6
Minorities/Disc ops	\$m	10.8	-7.9	12.5	11.0
Reported earnings	\$m	28.4	-85.3	52.6	28.0
Adjusted earnings	\$m	13.3	-73.8	52.6	28.0
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	4.5	2.4
EPS (adjusted, fully diluted)	c	1.1	-6.3	4.3	2.3
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	123.0	99.6
Net change in working capital	\$m	-25.3	31.3	-23.2	6.0
Other operating items	\$m	4.3	-3.3	2.2	0.0
Cash flow from op. activities	\$m	46.4	-5.2	101.9	105.6
Cash interest	\$m	-3.3	-3.0	-1.7	-0.3
Cash tax	\$m	-9.7	-15.0	-29.4	-29.6
Capex	\$m	-30.8	-8.6	-11.3	-50.0
Other items	\$m				
Free cash flow	\$m	2.5	-31.8	59.6	25.7
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	-4.2
Net change in cash flow	\$m	15.6	-38.0	55.6	11.5
Opening net cash (debt)	\$m	9.8	25.4	-12.6	41.8
Closing net cash (debt)	\$m	25.4	-12.6	41.8	52.1

Balance sheet		2019A	2020A	2021E	2022E
Year end:		Dec	Dec	Dec	Dec
Tangible fixed assets	\$m	376.9	362.7	349.0	366.5
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	148.5	142.5
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	76.5	62.8
Capital employed	\$m	631.8	539.5	583.2	581.9
Gross debt	\$m	52.8	56.5	35.1	11.0
Net pension liability	\$m	0.0	0.0	0.0	0.0
Shareholders equity	\$m	494.3	412.6	465.2	481.1
Minorities	\$m	84.7	70.4	82.9	89.7
Capital employed	\$m	631.8	539.5	583.2	581.9

Growth analysis		2019A	2020A	2021E	2022E
Year end:		Dec	Dec	Dec	Dec
Sales growth	%	4.9%	-84.0%	628.3%	-0.2%
EBITDA growth	%	28.5%	-147.7%	470.6%	-17.4%
EBIT growth	%	47.7%	-255.9%	279.9%	-28.1%
PBT growth	%	106.2%	-298.0%	270.9%	-33.0%
EPS growth	%	135.2%	-656.7%	168.7%	-46.8%
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%	55.0%	48.8%
EBITDA margin	%	32.2%	-96.0%	48.8%	40.4%
EBIT margin	%	16.1%	-156.8%	38.7%	27.9%
PBT margin	%	14.0%	-173.6%	40.7%	27.3%
Net margin	%	6.1%	-213.4%	20.9%	11.1%

Cash flow analysis		2019A	2020A	2021E	2022E
Year end:		Dec	Dec	Dec	Dec
Cash conv'n (op cash / EBITDA)	%	68.8%	n/m	82.9%	106.0%
Cash conv'n (FCF / EBITDA)	%	3.8%	96.0%	48.5%	25.8%
U/lying FCF (capex = depn)	\$m	-1.4	-44.2	45.4	44.2
Cash quality (u/l FCF / adj earn)	%	-10.8%	59.9%	86.4%	158.1%
Investment rate (capex / depn)	x	0.9	0.4	0.4	1.6
Interest cash cover	x	14.1	n/a	60.9	414.1
Dividend cash cover	x	n/m	n/a	n/m	2.6

Working capital analysis		2019A	2020A	2021E	2022E
Year end:		Dec	Dec	Dec	Dec
Net working capital / sales	%	78.0%	385.8%	59.0%	56.7%
Net working capital / sales	days	285	1,408	215	207
Inventory (days)	days	187	1,244	157	161
Receivables (days)	days	148	392	113	103
Payables (days)	days	50	228	54	57

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%	6.0%	1.9%

Capital efficiency & intrinsic value		2019A	2020A	2021E	2022E
Year end:		Dec	Dec	Dec	Dec
Adjusted return on equity	%	2.7%	-17.9%	11.3%	5.8%
RoCE (EBIT basis, pre-tax)	%	5.5%	-10.0%	16.7%	12.0%
RoCE (u/lying FCF basis)	%	-0.2%	-8.2%	7.8%	7.6%
NAV per share	c	42.2	35.3	39.8	41.2
NTA per share	c	37.5	30.9	35.2	36.5


Gemfields – Investment case

- **Long mine life at both assets:** 20 years at Kagem and 12+ years at Montepuez.
- **Premium products:** Gemfields is the only large-scale ruby and emerald producer, producing a consistent supply of high-quality and well-sorted material.
- **Ruby expansion:** Both markets have growth potential, especially the ruby market, which has the potential to grow >50%. This will be driven by construction of a second wash plant at Montepuez, expected to take place during CY22.
- **Stable pricing of coloured gems:** Unlike diamonds (a larger and sometimes over-supplied market), coloured gem prices have been stable and rising during Gemfields' 12-year history.
- **Established brand:** Gemfields is the only significant coloured gemstone producer. There are several juniors (eg Fura Gems) looking to emulate Gemfields, but with a very different (earlier stage or smaller) asset bases.
- **High margin:** Both mines are high margin, in particular the Montepuez ruby operation, which requires no blasting or the hand cobbing which is needed at Kagem.
- **Dividend expected:** We expect a maiden dividend to be declared during FY22, most likely at the FY21 results announcement in March.

Valuation

- **Risk models:** Our mine models are based on independent mining schedules for the two mines.
- **Fabergé and Sedibelo:** We use balance sheet values for Fabergé and Sedibelo.
- **G&A cost:** We also include -ve £190m to account for corporate and Fabergé G&A costs.

Gemfields – valuation

	US\$	£
Montepuez NPV	357,943,246	265,143,145
Risk factor	10% 	10%
Montepuez NAV	322,148,922	238,628,831
Kagem NPV	278,452,652	206,261,224
Faberge NAV	33,400,000	24,740,741
Sedibelo	25,000,000	18,518,519
G&A	(256,568,912)	(190,051,046)
TOTAL NAV	402,432,661	298,098,268
Shares in issue (m)		1,169.5
Share price target		25

Source: finnCap

Gemfields – Company overview

GEM – Company overview

Company Activities & Operations

Gemfields is a gemstone mining company with operations in Zambia and Mozambique. Its Zambian mine Kagem produces emeralds, the Montepuez mine in Mozambique produces rubies. Rough stones are then sold by auction to the international market. Gemfields also owns the Fabergé luxury goods business which is steadily rebuilding the Fabergé brand, manufacturing and selling a range of high-end products including watches, jewellery and objets d'art.

Company Strategy

To maintain consistent, profitable, long-term production at the two producing mines.

Key Products/Services

Product	Description
Rough ruby	Mined, cleaned and graded but uncut emeralds
Rough emerald	Mined, cleaned and graded but uncut rubies
Fabergé products	Wide range of high-end luxury merchandise

Management and Board

Name	Description
Martin Tolcher	Chairman
Sean Gilbertson	CEO
David Lovett	CFO
Adrian Banks	MD Product & Sales
Patrick Sacco	NED (Assore)

Company's Stated Objectives

Timing	Description
Short term	Pay a dividend
Medium term	Build a second washplant at Montepuez
Medium term	Successfully move Fabergé to profitability
Medium term	Divest Sedibelo
Long term	To diversify into other coloured gemstones - albeit likely to be smaller scale

Share Price Drivers

Probability	Description
High	Declare maiden dividend and expand ruby production
High	Publication of strong FY21 results in March
High	Expansion of ruby production and sales - from FY23
Low	Share buyback

Upcoming Events

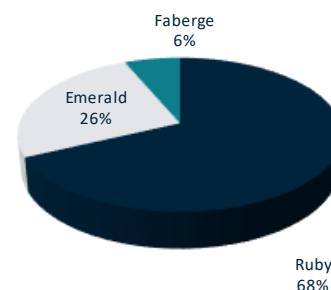
Date	Description
Mar-22	FY21 results

Recent Corporate Action

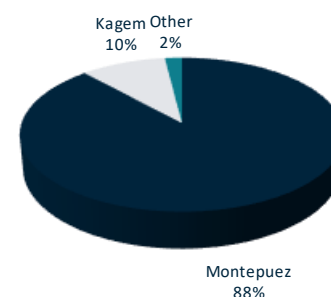
Date	Description
14-Feb-20	AIM listing - first day of trading

Source: finnCap

Split of FY 2022E Revenues:



Split of FY 2022E Capex:



Major Shareholders

Name	%
Assore International	26.6%
Rational Expectations (Pty) Ltd	9.0%
Oasis	8.1%
Ophorst Van Marwijk Kooy Verm'heer	7.7%
Fidelity International	5.9%
Solway Finance Limited	5.8%
Van Lanschot Kempen NV	3.4%

Other Information

Website: www.gemfieldsgroup.com
Location of HQ: London