Monthly Update

31 July 2023

Intelligent Investor Australian Equity Growth Fund (Managed Fund) (ASX:IIGF)

Issued by
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"Some people get rich studying artificial intelligence. Me, I make my money studying natural stupidity."

— Carl Icahn

The fund increased 2.0% during July compared to the market's 2.9% return. As there were no changes to the portfolio nor any major result announcements as we prepare for reporting season, let's dig into one of our largest holdings, **Mineral Resources**, which did release important news.

Best known for its crushing business, lithium first hogged the limelight when Mineral Resources sensationally sold half its Wodgina mine for $1.5bn in 2018.

MinRes had bought the mine for less than $100m just a few years earlier in an example of the guile that has characterised the business for years.

MinRes utilised all that guile to access equity in several processing facilities, including a stake in a Chinese processing plant, and equity in a WA based plant that would convert raw material from the Greenbushes mine. Both stakes have now been relinquished.

Performance (after fees)

	1 mth	3 mths	6 mths	1 yr	S.I. p.a
II Australian Equity Growth Fund	2.0%	1.2%	-5.7%	0.2%	12.4%
S&P ASX 200 Accumulation Index	2.9%	2.0%	1.2%	11.7%	12.3%
Excess to Benchmark	-0.9%	-0.8%	-6.9%	-11.5%	0.1%

Inception (S.I.): 5 October 2020

Fund overview

The Intelligent Investor Australian Equity Growth Fund is a concentrated portfolio of 10 - 35 Australian-listed stocks. The Portfolio invests in a mix of large, mid and small cap stocks, focusing on highly profitable industry leaders that have long-term opportunities to reinvest profits at high rates of return.

5+ yrs
Suggested investment timeframe

10 - 35
Indicative number of securities

Risk profile: High
Expected loss in 4 to 6 years out of every 20 years

S&P/ASX 200 Accumulation Index
Benchmark

Investment fee
0.97% p.a.

Performance fee
Nil

Key Points

- Another change to lithium assets
- No direct processing ownership
- Plenty of growth options remain

MinRes will now have control over its 50% share of spodumene from Wodgina and its second mine, Mt Marion, without equity in any processing plants.

This might sound like a step backwards, but MinRes is working towards a specific goal and this might yet be the best path forward.

Endgame

The business wants to build an integrated lithium business that mines raw material at Wodgina and Mt Marion and processes it into hydroxide in WA. Management has hinted that Plan B would be to seek another Asian host for processing, but the aim is to own both raw materials and processing plants. Doing that will capture mining and processing margins, generating far more value.

There is sense in the plan. MinRes has always aimed to capture margin across the value chain. It uses wholly owned crushing, logistics, transport, camps and services at its own mines, so the lithium plan would only continue that tradition.

Over time, this approach has generated sensational returns. MinRes has compounded earnings by close to 20% per year for almost 20 years. That sensational track record has earned our trust and patience.

The new deal has two immediate impacts. MinRes will receive a US$400m cash payment for its stake in the Kemerton plant and it won't have to contribute US$660m for the Chinese plants.

With MinRes currently expanding its iron ore operations, a $1.5bn balance sheet improvement is welcome. It does, however, come at a cost.

Downside

MinRes was expected to produce decent quantities of lithium hydroxide within the next few years through its ownership of processing plants. It will instead pay third parties to process spodumene and sell a lower value spodumene concentrate. Margins will be significantly lower as a result and there isn't a clear path for owning processing plants.

Management noted that costs and risks of native Chinese processing were prohibitive and that it was still seeking Australian processing options. It will take 5-7 years to find, fund and build a processing plant so processed lithium output is unlikely to be significant before the end of the decade.

In the meantime, Spodumene production will be significant, potentially rising to 900,000 tonnes of concentrate within three years if targets from Wodgina and Mt Marion are met.

If we assume spodumene concentrate prices of US$3,000 a tonne – they are currently about US$5,000 a tonne – MinRes should comfortably generate operating profits of over $2bn annually as a spodumene producer. That would probably be worth about $10bn, or just over $50 a share.

We are confident that production of processed hydroxide will eventuate, but we're treating hydroxide revenue as an option for now.

Beyond lithium

With so much attention to the lithium business, it's possible the rest of MinRes is being ignored.

The mining services division remains key and continues to grow volumes at over 20% per year. We reiterate our view that it is worth $30 a share with operating profits of over $800m per year expected within three years.

Earnings from iron ore ought to accelerate meaningfully despite expected lower prices.

Production will double to 36m tonnes within two years as the Onslow project is completed. Output could double again and costs should halve.

Less well recognised is the value of the bourgeoning gas business. MinRes has been coy about its size, but the business appears to have stumbled across one of the largest domestic gas discoveries in years. This is ideal feedstock to power future processing plants.

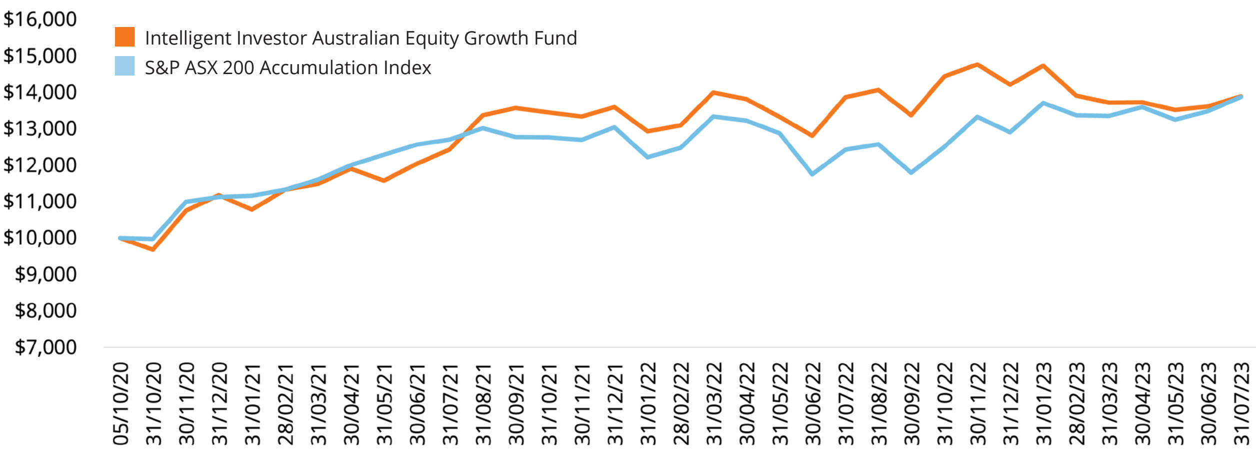
The flip flopping of lithium assets has resulted in less processed output and lower immediate margins, and that might concern some investors. We make two points against such concerns. Firstly, MinRes is so much more than a lithium miner and significant growth options are being pursued across the business.

More importantly, the flexibility to change a deal, to do something different, and to switch strategy is the strength of the business. Most management teams would view change as a weakness and would be worried about keeping their jobs. Here, we see management as pursuing the best deal possible even if it means short term pain.

MinRes founder and major shareholder, Chris Ellison, made clear he would rather pay higher initial capex for an Australian plant, and have lower ongoing costs with greater certainty, than pursue lower costs in the short term and accept higher risks. This is what makes MinRes a great business; a commitment to the long term. It is vanishingly rare.

Please get in touch if you have any questions on **1300 880 160** or at **info@intelligentinvestor.com.au**

Performance since inception



Inception (S.I.): 5 Oct 2020

Asset allocation

Materials	16.51%
Consumer Discretionary	15.75%
Cash	12.10%
Financials	12.08%
Information Technology	11.66%
Health Care	10.90%
Energy	6.94%
Industrials	5.93%
Real Estate	3.19%
Communication Services	2.73%
Utilities	2.22%

Top 5 holdings

RPMGlobal Holdings (RUL)	6.60%
Auckland International Airport (AIA)	5.93%
New Hope Corporation (NHC)	4.88%
CSL (CSL)	4.52%
Resmed Inc (RMD)	4.21%

Fund Stats

Distribution yield	6.17%
Net asset value	$2.7830

All tables and chart data is correct as at 31 July 2023