Value Investor INSIGHT

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The Leading Authority on Value Investing

Precious Metals?

There's a demand narrative for platinum group metals that doesn't paint a pretty picture for the miners of such metals. Focusing on the supply side of the equation, however, Hosking Partners' Django Davidson has an alternative view.

The capital-cycle investing approach followed by the U.K.'s Hosking Partners serves its principals' contrarian instincts, says founding partner Django Davidson, pointing them toward industries starved for capital and where supply is constrained, at a time when that dynamic may sow the seeds of cyclical recovery. "Demand is often storytelling," he says, "but supply is measurable and unbiased and we think is a great window into the future."

A case in point today, he says, is the global industry for platinum group metals [PGMs], consisting primarily of platinum and palladium. Some 65% of all PGMs mined are used as catalysts in internal-combustion-engine [ICE] vehicles, playing a key role in reducing harmful emissions. The broader narrative, however, is that electric-vehicle adoption is a material negative for PGM demand. That narrative combined with weak new-car sales and continuing automotive supply-chain issues have helped send PGM prices to generational lows. Platinum, historically priced on a one-to-one relationship with gold, at around $980 per ounce today is barely one-third gold's current price.

As is the case with many mined commodities, capital spending by PGM miners has been dramatically curtailed over the past decade. Part of that reflects newfound discipline after a period of profligate spending, but it also reflects the fact that 90% of primary PGM supply comes from South Africa, Russia and Zimbabwe, not highly favored destinations for capital investment. Davidson estimates that the cumulative capex "underspend" in the industry is equal to the combined market cap of listed South African PGM miners, making the bar to new supply should PGM prices rise extremely high.

His case then for PGM miners is that prices will rise as supply continues to increasingly fall short of demand and is very slow to correct – he estimates PGM prices would rise 50% from current levels before any substantial new capacity is added. He also argues that PGM demand may well surprise on the upside, putting further upward pressure on PGM prices. That would be true if the growth in electric-vehicle penetration slows – which is already happening in the U.S. – and/or if hybrid vehicles continue to take share, given that PGM content in hybrid vehicles is some 15% greater than in ICE cars.

To take advantage of this opportunity Hosking Partners has taken a "basket" approach, owning five stocks: **Anglo American Platinum**, **Impala Platinum**, **Northam Platinum**, **Sibanye Stillwater** and **Sylvania Platinum**. Each has its own unique characteristics, but all would benefit from rising PGM prices. "Mining companies have in-

From the Ground Up

If he's right that global supply/demand dynamics for platinum group metals [PGMs] are likely to lead to PGM prices returning more to historical norms, Django Davidson believes this basket of stocks could increase 3-5x in price and still trade at mid-single-digit P/Es.

Company	Ticker	Stock Price	52-Week		Market Cap ($mil)	Annual Revenue ($mil)	Net Margin	Dividend Yield	Largest Shareolder
			Low	High					
Anglo American Platinum	JSE: AMS	ZAR 628.07	ZAR 506.95	ZAR 876.75	$8,890	$6,041	10.4%	3.0%	Anglo American Plc (67.4%)
Impala Platinum	JSE: IMP	ZAR 97.60	ZAR 56.86	ZAR 129.86	$4,731	$4,655	(-20.0%)	0.0%	Public Inv Corp [South Africa] (17.7%)
Northam Platinum	JSE: NPH	ZAR 120.58	ZAR 88.87	ZAR 152.86	$2,533	$1,658	5.8%	1.2%	Public Inv Corp [South Africa] (20.4%)
Sibanye Stillwater	JSE: SSW	ZAR 17.20	ZAR 14.00	ZAR 27.38	$2,623	$5,836	(-48.6%)	0.0%	Public Inv Corp [South Africa] (15.0%)
Sylvania Platinum	AIM: SLP	£0.48	£0.39	£0.73	$153	$82	8.5%	4.2%	Africa Asia Capital (10.5%)

Sources: S&P Capital IQ, company reports, other publicly available information dividual operational and geological risks on top of any number of political risks," Davidson says. "If we're approximately right on the cycle with PGMs, we don't want to end up being precisely wrong by having all our eggs in one basket."

The potential upside? Miner results tend to be levered to the behavior of underlying commodity prices. In this case Davidson resists predicting the scale and timing of any PGM price rebound, but estimates that if prices for things like palladium returned to their 100-year ratio with gold, the stocks in the basket could appreciate 3-5x and still trade at mid-single-digit P/E multiples. Capital returns through dividends, he says, would likely add materially to the upside from there. VII