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Rich race

October 14, 2009

PORTFOLIO POINT: As three big players vie for a key position in this lucrative mineral, local stock investors can follow the money through a selection of listed stocks.

What do West Australian tycoon Gina Rinehart, former BHP Billiton chief executive Brian Gilbertson and Ukrainian billionaire Gennadiy Bogolyubov have in common? Apart from piles of money of course. They all have exposure to manganese – one of the world’s dullest minerals – and you might want to begin taking an interest in the subject too.

Rinehart, Australia’s richest woman, Gilbertson, a former head of Australia’s biggest miner, and Bogolyubov, Ukraine’s richest man, see manganese as profitable exposure to government-led economic stimulus spending, especially in China.

Because of its unique properties, manganese is an essential ingredient in making steel “long products”, such as girders and beams used in the construction industry.

After a spectacular price collapse last year, from more than \$US15 to about \$US4 a tonne, the manganese price is rising strongly; at about \$US6 it is already comfortably above its long-term average of the previous 20 years.

Three recent events highlight the activity of the three rich manganese players; the three Australian-listed manganese stocks worth considering make the symmetry complete.

The local manganese stocks are:

- OM Holdings (OMH), owner of the Bootu Creek mine in the Northern Territory and a company in which Bogolyubov has a 12% stake.
- Shaw River Resources (SRR), an explorer with three manganese projects in the Pilbara region of WA.
- Spitfire Resources (SPI), a small explorer, also with exploration assets in WA, close to the proved-up Woodie Woodie manganese mine.

A fourth possible entry point is Mineral Resources (MIN), a mining services contractor business with growing exposure to manganese, which includes a recent deal to acquire an interest in the manganese assets of the copper explorer Sandfire Resources and a deal to contract-mine manganese owned by Rinehart at Nicholas Downs (formerly Balfour Downs) in WA.

The Nicholas Downs deal represents the start of a second mine for Rinehart, the heir to an estate left by her father, the late Lang Hancock. The first is a joint venture with Rio Tinto at the nearby Hope Downs iron ore mine.

The first shipment of manganese from Nicholas Downs is due to leave Port Hedland next April, with production rising to 40,000 tonnes a month.

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As interesting as it is to see Rinehart open a manganese mine, the major event in the mineral involves Gilbertson, OM Holdings and Bogolyubov. Two weeks ago, Gilbertson orchestrated the start of a deal designed to see the private company he runs, Pallinghurst, acquire a 22% stake in OM by selling it a big manganese deposit in South Africa in exchange for scrip.

The deal seems simple enough, and Pallinghurst is one of the mining world's better connected companies. As well as having Gilbertson in charge, the "co-investors" include South Korea's biggest steel maker, Posco, the investment bank Investec, and wealthy American minerals investor Hans Mende.

The twist in the tale is that two years ago Gilbertson and Mende fought Bogolyubov for control of Consolidated Minerals, and lost. Back in 2007 Gilbertson launched a complicated bid for manganese company Consolidated Minerals, valued at \$2.28 a share, with a premium of just 1¢. Then Gennadiy Bogolyubov arrived on the scene and started a bidding war, which took the stock to \$5.01 before his company Palmary won control.

Today Gilbertson and Mende have effectively stuck a spoke in Bogolyubov's corporate wheels by orchestrating the OM deal which, if completed, has the effect of making OM "the world's only pure-play manganese miner" but also dilutes the Ukrainian's stake in OM to 9.3%, an event that will not please a classic post-Soviet era oligarch.

Translated these events mean that manganese as a commodity is "in play", with more developments certain to occur, which in turn means an uplift for all players in a game that is dominated by the world's mega miners.

Manganese is closely related to iron ore in more ways than one. It is geologically similar and often found close to iron ore deposits. Production is dominated by big mining groups such as BHP Billiton at Groote Eylandt in the Northern Territory, Vale in Brazil and Assmang and Samancor in South Africa.

However, global output is far less than iron ore because only small amounts are used in steel production. Last year, global production was estimated at 14 million tonnes, with high-grade deposits reported to be running low.

Despite playing second fiddle to iron ore, the profit margins from manganese can be enormous. Last year, despite the global slowdown, BHP Billiton's profit from manganese mining fell at a slower rate than most of its other commodities. Underlying earnings from manganese totalled \$US1.35 billion (down 17.9%) whereas petroleum earnings fell 25.5%, aluminium 86.9%, and base metals 83.8%.

The important investment clue in BHP Billiton's manganese report, one of the few publicly available in a very tight-knit industry, was that the recession-hit profit of \$US1.64 billion came from revenue of \$US2.5 billion – a margin of 54%, one of the highest profits on BHP Billiton's books.

It's the profit margin on offer as consumption of manganese rises in the construction-steel business that is driving Gilbertson, Rinehart and Bogolyubov deeper into manganese – coupled with the fact that high-grade deposits are running down.

That's why OM wears the hallmarks of a rerun of the Consolidated Minerals takeover struggle of 2007 during which bid and counter bid saw the stock double in price.

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At recent trades around \$1.68, OM is capitalised at \$820 million, and well above its 12-month low of 66¢. However, the stock has actually fallen from the \$1.81 it was trading before Gilbertson and his co-investors announced their proposed deal – and to which Bogolyubov is yet to reply.

Either OM is on the way to becoming Gilbertson's manganese vehicle, with mines in Australia and South Africa making it an interesting investment proposition, or Bogolyubov will launch a counter-bid to ensure an ongoing supply of high-grade manganese for his Ukrainian steel interests, in which case it is an even more attractive proposition.

As for the other local players, Shaw River and Spitfire, both are exploration plays and fall into the high-risk (high reward?) "tiddler" category. Each has the potential to either develop a mine or be acquired as the manganese game develops a head of steam.

Shaw River's share price has risen strongly since April, from a low of 3.5¢ to 18¢, which capitalises the stock at \$34 million.

Spitfire has been a slower mover, rising from 5¢ to recent trades at 8.3¢ and a market value of \$6.3 million.

Mineral Deposits is a diverse mining contracting, which is also developing a number of its own mine assets. It suffered a precipitous fall from more than \$7 a share in late 2008 to a low of \$1.53, but has recently been in strong recovery mode, trading close to its 12-month high of \$7.30 and a market value of \$930 million.

There are no investment routes into the other business assets of Bogolyubov or Rinehart.