Gleneagle Asset Management Gleneagle Investment Fund (GT Momentum Portfolio)

May 2021 Review

The GT Momentum Fund declined by 14.38% in May, with several factors affecting the performance over the month.

Firstly, I would like to stress that it is never pleasing to report a result such as the one above and although it is an extremely frustrating result, as a significant investor in the fund I am not overly concerned. This is primarily because I understand what factors actually affected performance, the pipeline of investments made in the fund that will bear fruit and that declines (volatility) such as this are part of the process of the pursuit for even larger returns. In my 25-year trading career, there have been several circumstances where such stumbling blocks have occurred and each time these have only been fleeting. Very few professional athletes win championships without a single loss or hurdle, and likewise, we will experience them too on the journey to future profits.
So let me explain what the main contributors to the decline were.

The portfolio at any given time is broken down into several strategies:

1) Short-term active trading
2) Medium to long-term thematic based investing
3) Unlisted investments that are primarily pre-IPO or convertible bonds

In May, the short-term active trading portfolio registered its first monthly loss since late 2019. The short-term trading strategy usually produces a profit that helps smooth out the swings of the longer-term thematic based investments. Last month, it failed to do that, and I will raise my hand and state that the combination of a "choppy" market and being caught out with one particular news event impacted the final return. On 5 May, Near Map (NEA) issued a profit upgrade and positive outlook and, being a business that we like and have traded successfully in the past, we began buying expecting this to be the trigger for a significant bullish re-rating. The share price reaction certainly gave that impression surging 14% that morning - a great start. However, just 90 min later, NEA entered a trading halt and the following day stated that it had been named in litigation for a breach of a patent in the USA. The share price as a result dropped 23% and while we were quick to exit, it still ruined our month's short-term trading returns. The choppy nature of the market, with very few breakouts and trends persisting overt the month, meant that momentum based trades were unable to add any value. Overall, the short-term trading portfolio cost the fund 3% in May. In context, there have been months where the short-term trading strategies have contributed north of 10% in a month.

Many of our medium and long-term thematic investments experienced weakness in May as the resources and renewable energy revolution trend took a pause in its recent trajectory. Last month we noted that a new investment, Energy World Corporation (EWC), that presented a very unique opportunity, was added to the portfolio where we participated in the underwriting of the entitlement offer. This was done at 8c and it quickly jumped 68% in a matter of days before ending the month +47.3%. As is often the case, when such gains are seen, when the underwriting stock is issued to the new shareholders there are some who wish to bank some quick profits (and not remain in the trade for the longer-term) and the stock can retreat back towards its issue price which was the case for EWC in May. And although it dropped 23% in the month, we are still up on our investment but the monthly drop dragged the fund lower by 2.5%.

Some investors may be asking why we didn't sell and buy back in to begin with, we didn't believe EWC would retreat as far as it has but nonetheless that is something we can't control. However, when making such decisions, it is important to understand the consequences of selling out where the share price doesn't retreat but instead continues to appreciate. Is it more painful to miss out on future returns or give back existing returns? Naturally, that depends on the individual stock and in the case of EWC, as we highlighted last week, we invested at a valuation of $161 million when compared with net assets of the company of $982 million. It would be difficult to give a rational explanation for selling out and seeing the share price continue to strengthen.

Similar circumstances applied to Rumble Resources (RTR) which surged 600% in April after announcing strong drill results for its Earaheedy Zinc-Lead-Silver Project. Having been a previous investor in Rumble, we quickly built a position for the fund in the stock, believing this is likely to be a significant new major discovery that could see the share price (on further strong follow-up drill results) at $2.00 per share. The downside to such opportunities in new discoveries is the share price ride can swing by extreme amounts. It peaked at 80c in the month and ended at 54.5c – a drop of 32%! Rumble is one stock which we have been trading more actively instead of buy-and-hold, but still the retreat in the share price cost the fund 2%.

Another source of pain for the fund in the month was American Pacific (ABR) which is in the process of developing the Fort Cady borate project in Southern California, USA. This has been a Company I have supported since March 2019 at 19c, representing an increase of 1200% for investors up until the end of April where it closed at $2.41. Unfortunately, the Company last month informed the market that there was a change in strategy that would combine the current staged expansion plans into one larger project that would provide a more attractive investment proposition for US investors as ABR also pursues a US-listing. In short, this would delay the current plans by about six months and the market took a sword to the share price as a result. We strongly believe the resulting decline from $2.40 to $1.45 was a complete over reaction. Speaking with management and other institutional shareholders, we increased our shareholding in the Company between $1.20 and $1.40. The benefit to this is it has reduced the equivalent end-of-month price to which we claw back last month's drop - from $2.41 to $1.70. ABR annoyingly cost the fund 4%.

Finally, a reduction in our other long-term faithful holdings also retreated marginally over the month but collectively contributed to the remainder of the declines – approximately 3%. A very frustrating case of several stumbling blocks in the month of May with very little to offset that.

Market reactions in May also proved difficult to fathom as well, which added to our frustration and none better reflected than the performance of Bluescope Steel (BSL) – one of our go to favourite trades that reflects the increasing infrastructure demand globally. Bluescope has been a core holding in the fund for this very reason and we were rewarded when the Company issued a profit upgrade on the 27Th April where the share price rallied from $22 to $24. It ended May at $21.23 after touching a low of $19.87, 10% below the price BEFORE the profit upgrade. I don't see us anywhere near the end of the bull cycle in steel, commodities or infrastructure development, so price action like this is difficult to reconcile and as result with many markets in a washing (or distribution) cycle we tend to reduce our trading activity as result.

On a brighter note, we have updates regarding several of our pre-IPO investments. Last month we highlighted our sizeable investment in Infinite Blue, Australia's first commercial green hydrogen producer via its Arrowsmith plant in WA. The $10 million pre-IPO round was oversubscribed within 22 hours and we were very fortunate to have received our full allocation, making the fund a Top 20 shareholder. The IPO has now been slated for September 2021 and will be priced at a 100% uplift from our investment price. Considering the gains of other ASX listed hydrogen hopefuls which have appreciated north of 300% we are extremely excited about the potential for Infinite Blue post its $100 million IPO raising. Investors who wish to know more can read this article (Click Here).

Another pre-IPO investment was made in MyRewards which is also slated to IPO in a few months. While this was a significantly smaller investment than Infinite Blue, it equally has the potential to return us multiples on our original investment. MyRewards is a fast-growing provider of shopping, loyalty and rewards solutions for businesses and consumers and have grown to be one of Australia's largest providers of loyalty programs. MyRewards connects 4.6 million customers with over 100+ corporate clients with access to over 4,500 products. We helped fund a small acquisition for the Company prior to the IPO. With a valuation of just $15 million our investment in MyRewards compares very favourably with ASX-listed Cash Rewards that trades at a 500% higher valuation despite having similar revenue numbers and operates with a significantly larger net loss. I would expect MyRewards to trade at a similar valuation to Cash Rewards post its ASX listing.

Finally, our last investment this month was into a small IPO called Locksley Resources which is being spun out of ASX-listed nickel producer Mincor Resources (MCR). Locksley will house the copper assets (Tottenham Project) previously held by Mincor that exits in the Lachlan Fold Belt of New South Wales, surrounded by many successful deposits. After speaking with management to obtain a deeper understanding of the geology, the Tottenham project has significant low-risk potential given the discovery work that had been done by Mincor in the past. With an IPO market-cap of just $11.2 million this is a Company that could really surprise many considering that similar copper developers are trading at valuations of $35-$75 million. Again, the demand for this stock and the drilling activity planned could see this of immense interest after it lists in early July.

As I have done in the past, whenever, there is a dip in the returns of the fund I look to increase my investment in the fund and I have done the same again this month. My confidence in our processes, trading strategies, pipeline of upcoming IPO's gives confidence that such declines in the NAV of the fund are only temporary. More importantly I have utmost confidence in our ability to quickly adjust to market changes and reflect on where we have made mistakes and rapidly implement measures to reverse course.

I always assess disappointing outcomes across the following two measures – poor execution or wrong ideas. Poor execution can be quickly improved and adjustments can be made (buying pullbacks rather than breakouts for example) however, wrong ideas – that is investing in completely the wrong sectors and markets – is a lot more difficult to overcome. After all, even perfect execution with wrong ideas will still lead to losses. I know this month's performance is more of a reflection of poor execution and unfortunate timing in reporting and not wrong ideas. Because of this I continue to be optimistic in our strategy, portfolio and the year ahead.

As I noted last month, I will also be holding a monthly webinar for those interested in understanding our outlook and portfolio in more depth and to ask any questions

Until next month,

Gregory Tolpigin Portfolio Manager
Gleneagle Securities (Aus) Pty Ltd