Investment & NTA Update

31 October 2021

NGE Capital Summary

ASX ticker	NGE
Share price (31 Oct 21)	$0.760
Shares outstanding	36,169,127
Market cap	$27.5m
NTA per share before tax	$0.920
NTA per share after tax	$0.975
NTA before tax	$33.3m
NTA after tax	$35.3m

Overview

NGE Capital Limited is an internally managed Listed Investment Company which allows investors to gain exposure to a concentrated, high conviction, actively managed portfolio of financial assets. NGE primarily focuses on listed ASX and international equities, with the aim of generating strong risk-adjusted returns over the medium to long term.

Board & Management

David Lamm
Executive Chairman &
Chief Investment Officer

Adam Saunders
Executive Director &
Portfolio Manager

Ilan Rimer
Non-Executive Director

Les Smith
Company Secretary &
Chief Financial Officer

Contact Details

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Net Tangible Assets Per Share

	31 Oct 2021	30 Sep 2021
NTA per share before tax	$0.920	$0.914
NTA per share after tax	$0.975	$0.969

NTA Per Share Performance Summary

1 month	Year-to-date	Last 12 months	Since inception[1] (p.a.)	Since inception[1] (cum.)
0.7%	17.6%	38.3%	12.8%	80.4%

Note: Returns are net of all expenses.
1 From 30 Nov 2016, the date on which NGE became a LIC.

Portfolio Composition

Company	Ticker	% of NTA
Yellow Cake plc	LSE:YCA	17.8%
Metals X	ASX:MLX	11.1%
Geo Energy Resources	SGX:RE4	10.5%
Evolve Education Group	ASX:EVO	6.0%
Sprott Physical Uranium Trust	TSX:U.UN	4.5%
Allegiance Coal	ASX:AHQ	4.3%
International Petroleum	TSX,STO:IPCO	2.0%
Base Resources	ASX:BSE	1.8%
Consorcio ARA	MEX:ARA	1.6%
Silver ETFs	SILJ, SLV, SIL	1.6%
Austin Engineering	ASX:ANG	1.5%
Undisclosed – 3 positions	Listed	2.0%
Net cash and other		35%
Total		100%

Unrecognised Tax Losses

The Company has ~$44 million of Australian unused and unrealised losses available as at 31 October 2021. In the aggregate these losses equate to a potential future tax benefit of ~$11m or ~$0.31 per share (of which only $2.0m or $0.055 per share is recognised in our after tax NTA). The Company has received tax advice that these losses are available to be offset against future tax liabilities so long as NGE continues to satisfy the continuity of ownership test as set out in Divisions 165 and 166 of the Income Tax Assessment Act 1997 (Cth).

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In last month's NTA Statement we mentioned that we had initiated two new positions during September, which we discuss today: **Evolve Education Group Limited (ASX:EVO)** and **Austin Engineering Limited (ASX:ANG)**.

We acquired 2.35m shares of **Evolve Education Group (ASX:EVO)** at an average price of ~A$0.70 per share. We settled on our initial holding size as the stock is illiquid.

Evolve is a provider of Early Childhood Education (ECE), operating 111 childcare centres in New Zealand and 23 in Australia. We think the shares have been oversold, despite investors' well-founded concerns around the historical and continuing underperformance of the NZ centres, and a current dearth of ECE qualified teachers in NZ (which in addition to staff shortages is leading to wage pressures). A $21.7m placement done at A$1.10 per share in March to fund future centre acquisitions in Australia, just prior to an earnings downgrade, is also likely to have lost support for the stock.

The company was founded as a private equity-backed vehicle used to roll-up centres and rapidly gain scale. Whilst the business initially performed after its IPO in 2014, the loss of key personnel in 2017 precipitated a period of rapid deterioration of the business during 2017-2019, as the company cycled through 3 different CEOs in quick succession. Evolve took a NZ$107m impairment to goodwill in its FY19 accounts as average centre occupancy dropped from high-to-mid-80s to low-70s and the company engaged in heavy discounting to try and counter the slippage.

In May 2019, around the same time as the impairments, Evolve recapitalised the balance sheet by raising NZ$63.5m in a heavily discounted rights issue (NZ$0.64 per share on a post share consolidation basis). Evolve used the proceeds to pay down NZ$30m of debt and fund an initial expansion into Australia (NZ$25m). The company also initiated the New Zealand Turnaround Plan, which aimed to improve retention of customers, reduce staff turnover, reduce price discounting, drive better conversion of leads, and sell or close non-performing centres.

Current Managing Director, Chris Scott, stepped up from a non-executive role in August 2019. An experienced hand, Scott was MD of **G8 Education (ASX:GEM)** from 2010 to 2016. He has serious skin in the game, having accumulated a 16.4% stake in Evolve by spending ~A$35.0m at an average price per share of ~A$1.33.

As Covid-19 hit, Evolve was in the early stages of its turnaround. To get a sense of centre-level performance in NZ, we analysed the past two rating reviews done by the Education Review Office (ERO) on each of Evolve's NZ centres. We went back through four years of reports on the "My ECE" website to check for any license downgrades on each centre. We also reviewed the publicly available ERO reports on the 9 centres that were below a "well placed" rating or not "meeting all" criteria. Our assessment is that on the whole the NZ centres are performing to a satisfactory or better than satisfactory service standard. Of the centres that need improvement, our reading of the materials suggest that most problems identified are fixable, and could be addressed by a combination of:

- hiring better qualified staff and managers;
- providing additional training to existing staff on matters of curriculum, ECE regulations and childcare best practices; and
- implementing more rigorous centre procedures, including more frequent and rigorous staff evaluations.

Many of Evolve's centres have recovered well from previous negative ERO reviews.

The rewards for a successful turnaround are significant: every 1% boost to occupancy lifts NZ EBITDA by ~NZ$1.3m. NZ occupancy is running at ~69%. In rough numbers, the NZ business currently does ~NZ$18m centre-level EBITDA, with an additional ~NZ$8m of corporate overheads to service the centres.

The Australian business is having no such issues, and is firing on all cylinders with occupancy ~85%. All centres bar one are meeting or exceeding all seven quality areas of Australia's National Quality Standard. The Australian centres should earn ~A$12-13m of EBITDA, less ~A$1m of corporate overheads.

Combined, Australia and NZ should do ~NZ$21-22m EBITDA on the existing centre base assuming "business as usual", but the company is anticipating further acquisitions in Australia which could add a further ~A$5m of EBITDA (~A$20m to spend at an average acquisition price of 4x EV/EBITDA).

Capital structure		AUD	NZD
FX rate	AUD:NZD	1.0000	1.0487
Share price (31-Oct-21)	$	$0.85	
Shares out.	m	159.5	
Market cap	**$m**	**135.6**	**142.2**
Net debt	$m	-3.9	-4.1
EV	**$m**	**131.7**	**138.1**

Two recent acquisitions by UK-based Busy Bees, which is controlled

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by Ontario Teachers' Pension Plan Board, provide relevant valuation benchmarks for Evolve. In October Busy Bees finalised its acquisition of Think Childcare's (ASX:TNK) mature childcare centre business, with the Independent Expert valuing the Scheme Consideration at ~9.7x-10.9x EV/NTM EBITDA. Also in October, it was reported that Busy Bees had acquired NZ-based childcare operator Provincial for NZ$160m, with estimates suggesting the deal implied an EV/FY22E EBITDA of 9.1x-10x.

If we apply a valuation range of 8-10x EV/EBITDA to the company's FY22E EBITDA guidance, it suggests significant upside from the month-end price of A$0.85:

		Low		High	
Valuation		NZD	AUD	NZD	AUD
FY22E EBITDA	$m	23.0	21.9	25.0	23.8
EV / EBITDA	x		8.0		10.0
EV	$m		175		238
Market cap (implied)	$m		179		242
Value per share	**A$**		**$1.12**		**$1.52**
Upside	*%*		*32%*		*79%*

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During September, October and November, we acquired 2.50m shares (2.18m at month end) of **Austin Engineering (ASX:ANG)** at an average price of ~$0.22 per share. We settled at this relatively small holding as the stock is very illiquid.

ANG's main business is the design and manufacture of customised off-highway truck bodies for the mining industry. Truck bodies are the "trays" that sit on monster 100t+ trucks that haul iron ore, coal and other bulk materials from a mine. The company also manufactures mining buckets, water tanks and other ancillary products.

We were attracted to the company, which we had looked at several years ago, because the company has a new and experienced CEO, a small net debt position will likely be paid off by year end, loss-making and low-margin parts of the business are being sold off or wound up, and the company has been reducing overheads. The company is also undertaking a small capex program to improve manufacturing processes to improve labour efficiency, as labour represents ~60% of manufacturing expense.

According to management, in the past ANG had over-engineered its truck bodies using thicker steel, which made them more resistant to wear and tear but also very heavy. ANG now designs lighter bodies to maximise payload, which benefits its mining clients, but also results in higher replacement rates (3-5 year life vs 10+ years previously).

The company's cost-out program should result in realised overhead savings of ~$10m in FY22 (restructuring charges were taken in FY21 accounts), which is material on an EBITDA base of ~$20m. The $6.5m capex program this year to improve manufacturing productivity at the company's facilities in Kewdale, Perth and Batam, Indonesia is aiming to lower the cost of manufacturing truck bodies by up to 15% (i.e. a 25% boost to productivity on a 60% cost item). The margin improvements are expected to show up in FY23 results, and could improve EBITDA by a further ~$3m-5m p.a..

Capital structure		
Share price (31-Oct-21)	$	$0.22
Shares out. (diluted)	m	596.9
Market cap	**$m**	**131.3**
Net debt [1]	$m	10.2
EV	**$m**	**141.5**

[1] Pro forma for dividend paid 30-Sep-21.

We value ANG in a range of $0.28-$0.38, based on what we consider to be conservative earnings multiples:

Valuation		Low	High
FY22E EBITDA	$m	30.0	35.0
EV / EBITDA	x	5.5	6.5
EV	$m	165	228
Add: Asset sales	$m	11	11
Value per share	**$**	**$0.28**	**$0.38**
Upside	*%*	*26%*	*74%*

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During October we switched out of a portion of our holding in **Yellow Cake plc (LSE:YCA)** and into units of the **Sprott Physical Uranium Trust (TSX:U.UN)** whilst YCA was trading at a ~7% premium to NAV and SPUT traded at close to par. Net of transaction costs and slight timing differences, we gained a ~5% benefit in overall NAV. We may carry out further such trades in the future when the opportunity presents, as we think it makes sense to have a higher weighting in the larger and more liquid SPUT vehicle.

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During September, we sold down ~75% of our **Base Resources Limited (ASX:BSE)** holding. We currently hold ~1.95m shares. When we originally invested back in 2018, we were getting the Kwale mine's cash flows at a discount to our valuation, whilst gaining exposure to the undeveloped but world-class Toliara project in Madagascar for free. Since then, the Toliara project has been delayed due to a fiscal terms dispute with the Madagascan government, and Base has been unable to extend the mine life at Kwale as much as was hoped due to an unfavourable PFS on the North Dune and Bumamani mineral deposits. Base is currently scrambling to find more reserves to feed Kwale's plant, which may or may not be successful.

As Kwale's reserves are being depleted, Base's share price is implicitly attributing more value to Toliara. That is likely warranted due to its massive size and favourable economics, but the timing on resolution of the fiscal terms is unknown, and it will take at least another ~3 years and considerable risk from then before first ore is shipped.

We may decide to reinvest in the future as some of the uncertainties are resolved, but are happy to de-risk our investment in the meantime having pocketed ~28% of our original investment in dividends in addition to a ~16% capital gain on our sold shares.

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During the month we sold out of our remaining holding in **Vita Group Limited (ASX:VTG)**, resulting in a small overall profit on our investment.

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Announcement released to the market with the authorisation of:

David Lamm	**Adam Saunders**
Chief Investment Officer	Portfolio Manager