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## On the Sashimi Plate

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*"I have not failed. I've just found 10,000 ways that won't work."*

----- Thomas A. Edison

*"The whole problem with the world is that fools and fanatics are always so certain of themselves, and wiser people so full of doubts."*

----- Bertrand Russell

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*"Dear Clients,*

Port Lincoln, home of the legendary Australian horse ***Makybe Diva***, a three times ***Melbourne Cup*** winner, and the Australia Southern Bluefin Tuna industry. The Southern Bluefin Tuna is one of the most sought after delicacies in Japan, and many other places in the world. During the good old time 10 years ago, the wholesale price of the Southern Bluefin Tuna (SBT) was over \$20 per kg and we still could not find enough of it. One of the legends in the tuna industry Mr Hagen Stehr AO (nicked name ***Tuna Cowboy*** by the Japanese, see photo 6 ) thought it would be a good idea if we could farm it, it would be just like printing money as there was a \$10 per kg margin on the table.



*Makybe Diva in Port Lincoln*

Thus the listed company called ***Clean Sea Tuna (CSS)*** was born. The plan: get the huge wild tuna brood stock CSS owned to lay eggs, hatched them, then in three or four years' time you produce a 15kg to 20kg pricey and sought after tuna. Australia then would have a great tuna farming industry, making lots of money from export, and everyone would be happy. It sounds like a great idea. Our country never lacks adventurous entrepreneurial spirit.

The company first bought a couple of huge tanks (25m x 6.5m) from Denmark. Then it got the scientists to start the romantic love story: let the big wild brood stock tunas have babies. The task took three years, harder than expected, finally in 2008 they achieved the world's first production of aquaculture fertilized Southern Bluefin Tuna eggs and viable larvae under certain romantic conditions.



*Kingfish sashimi & sushi*

It took two years of trial to grow the larvae to hand sized fingerlings, but unfortunately the fingerlings were unable to survive and grow in South Australia seawater. Why? The scientists later thought the mystery could be the sea water in SA might be just too cold. The tuna fish we catch here in South Australia are actually born in the warmer sea water areas between the north west coast of Australia and Indonesia. When the fish swim to South Australia, they are already "teenagers" and are able to handle the chilling cold.

It was a great trial, the share price also had its time in the sun. It went over from \$0.50 listed price to over \$2 at one stage, but after a few rounds of capital raising and millions of dollar spent, the cash was pretty tight, the commercial reality looks still far away, it had to stop the program. We have been a keen follower of the story, though only a small investor. The company had great potential break through, both scientifically and commercially, but the end result was disappointing.

***So when we watch someone succeed, there is always someone else who has tried and failed, but we admired their spirit.***

So came the ***Plan B***.

When CSS started the STB research, it already had a kingfish farming business. The idea was that while it was pursuing the big dream (tuna farming which would provide a potential margin of

\$10 per kg comparing with kingfish \$2-\$4 per kg), the kingfish farming was the bread and butter.

This is the sequel of our South Australia trip in Nov 2015 (titled *Hill of Grace & the new Adventure*). The second leg of the tour was to Port Lincoln to see the CSS' *Hiramasa Kingfish* farming operation on an investor day tour.

The little *Qantas "private jet"* flew us over the magnificent South Australia coastline.

The day tour started on board a ship at Port Lincoln, where we were welcomed by the chairman Mr Paul Steere (a very nice man), Mr Hagen Stehr and the executive team. The ship took us out to the ocean to see the Kingfish growth cages. It was a magnificent operation and asset, with clean water and beautiful fish!

Then we hopped on a bus to the Arno Bay hatching facilities, a CSS owned 400 hectare property and facilities sitting on the beautiful coast just over 100km from Port Lincoln. It was an excellent facilities. We inspected the big kingfish brood stock and the millions of fish larvae. CSS has great techniques for producing food for the kingfish larvae.



*Kingfish, Salmon & Tuna sashimi plate*

Finally, of course, we were served the world's best Hiramasa Kingfish sashimi. But one delicious dish that surprised us most was: *White Hiramasa Kingfish Caviar*. Even though the caviar had not yet been commercialized, it may have a big potential and could put *CSS's name on the world's top menus*.

Under the former MD, Mr Craig Foster, the kingfish farming side made a solid return after a fish health issue in 2012 that almost destroyed SA kingfish farming (CSS thought it was caused by the

fish feed and is seeking compensation from the feed supplier), as the company entered into a new marketing stage after Mr Foster retired in January 2016, CSS appointed Mr David Head as the new MD. David, a former executive at Pepsi and Lion Nathan, has a strong track record.

David did some desk clearing and raised some money. We participated in the capital raising to support the company's turnaround strategy. But the current share price is still lingering around the historical low, we suspect that it is because as it is a small company, investors would expect to see the business improved more quickly, different from a large company that normally takes longer time, and at the current price it could become a takeover target, as happened last year to PBG, and now SPO.

At the current price (around \$0.04) we think the current enterprise value of around \$50 million is similar to a hobby farm price and more a reflection of the fish value in the ocean cages rather than its wonderful properties and outstanding facilities, not to mention its fish farming know how techniques and the research IP.

Why it could fall into other player's hand?

1. CSS has world class assets; it is at a great fish farming location, owns its own property and has a great facility. Would an overseas food company take a bite?

2. There are three Salmon farming companies listed on the ASX: Tassal (TGR), Huon (HUO) and newly listed New Zealand King Salmon (NZK). Interestingly, CSS's former chairman Mr Paul Steere is also a current director of NZK, and director Mr Nick Burrows was Tassal's former CFO. The company's new chairman Mr Terry O'Brian just started this week.

CSS might be a great fit for the listed salmon famers: first it offers diversification & synergy, both locations and products, like what's on the sashimi plate: salmon, tuna and kingfish. What a



great match! Secondly, CSS has over \$100 million accumulated tax losses, would this be valuable for others? As CSS has a weak balance sheet, would the company be able to progress much faster within a bigger corporation that is able to do more to utilise the Port Lincoln facilities?

As a CSS shareholder and a keen follower of the company, we hope the company can grow, improve its value, reach its dream potential, and help our country's economic growth.



*Photo 1: Teddy and Charley at Arno Bay facilities*



*Photo 2: Kingfish Larvae*



*Photo 3: Kingfish fingerlings*



*Photo 4: Clean Seas Tuna's fish grow-out pond*



*Photo 5: CSS team showing us Kingfish*



*Photo 6: Hagen Stehr and Nagae*



*Photo 7: Clean Seas Tuna hatchery<sup>2</sup>*



*Photo 8: Clean Seas Kingfish sea pens<sup>2</sup>*



*Photo 9: Clean Seas Kingfish sea pens<sup>2</sup>*

## *Talk around the Block Arcade Desk*

**Felicity:** TPG announced it is going to build the fourth mobile network in Australia, do you think it's taken on more than it can chew?

**Big foot Charley:** potentially. As we are TLS shareholders and many retail clients also own TLS shares through the TLS float, we might be biased by heart, this is obviously negative news for TLS and other telcos, but TPG is taking on a greater risk, even though, like Alibaba's Jack Ma said, "nothing is impossible".

Before it merged with iinet, TPG's core strength was as a very efficiency reseller, e.g. selling TLS, Optus copper/fibre line service (plus some of its own) but at a lower price given its lower cost base and the good skill of running business more efficiently. David has been very successful at doing that, you've got to admire him, but building a new mobile infrastructure, maintaining it and keeping it running nicely is a whole new game, even though TPG has made progress in Singapore. If we look at how much TLS, Optus, Vodafone Hutchison Australia (VHA) have spent, I think \$600 million is just not enough for it to have a good start. TPG plans to build 2000-2500 sites, reaching 80% of the population, currently VHA has about 5000 sites (reaching 96%), Optus about 6000 (98.5%) and TLS about 8500 (over 99%), You may argue that technology has changed, allowing TPG to build things more cheaply and better, but as we know you still need enough towers to cover enough area. If it doesn't work out well, as happened to VHA a few years ago, and you upset your existing customers, then you are in real trouble.

**Felicity:** with four players in the mobile sector now, what's the outlook for the industry?

**Big foot Charley:** it depends on which path they walk down. Normally four players hardly do well in one sector in Australia, other than the banking sector. In the airlines industry, we watched Ansett airline disappear. After Aldi and Cosco opened shop in

Australia, Metcash has been having a real hard time. We saw the merger of Hutchison and Vodafone a few years ago to improve their offering. TPG says that, as it has only 500k mobile customers and can be a price leader, fighting for market share, it is not always the case. As a starting point of \$2billion investment is a big commitment and, as we observed in the Woolworth's Master case, the fall out was pretty bad. Virgin Blue also took some blue from the fight with Qantas. I guess as the world is moving away from the fixed line to mobile, TPG wants to get into this growth area. On the other hand VHA also plans to expand into the fixed line business through the NBN network this year.

I think it might make sense for TPG and VHA to merge, as TPG does not need to waste resource duplicating VHA's towers, and the merged company could use the combined funds to improve its technology and offering, with benefits for consumers as well. So the \$600 million plan could be like buying a chair at the negotiation table.

***Felicity:*** do you think the mobile phone companies are charging too much or not enough?

***Big Feet Charley:*** if you look at how much the current three mobile companies have invested to buy the spectrums, build the networks and do the maintenances, I don't think as a whole, they make too much money out of it. VHA has been losing money. But society and industry should understand that in the long run, companies need to charge a fair price for their services, so that shareholders get a reasonable return and the company can reinvest, and in the longer run there may be greater benefits for everyone.

Consumers and the Internet companies have enjoyed most of the fruits of the infrastructure spending by the telcos.

Nowadays people rely on mobile phones more than ever. We use the phone not only to call but also to chat through WhatsApp or



We Chat, and for watching videos. We also use the phone to pay bills. The smart phone has taken on more roles than before.

***Felicity:*** finally, as you are a keen follower of TLS and called it a “**golden goose**”, what do you think of it now?

***Big feet Charley:*** haven’t you eaten some nice “roasted goose” already (just joking)? If it cannot lay “golden eggs” any more, it may be still able to lay some “silver eggs”. Maybe it can invest cleverly and generate a steady income, for example, it could use its strength to partner with the Government or hospital operators to grow the healthcare service offering and generate a new source of steady income. It also has the ability to conduct an on market share buyback, so “ **be alert, but not alarmed**”.

*After a break we have a brief chat on the new Budget*

***Teddy the Bear:*** Nagae, what do think about the Budget?

***Nagae the Cat Maro:*** it looks like a good one to me, even though our boys are going to pay more for their university fees. I would like the Government to spend more on the “soft infrastructures” than building more roads we rarely use. For example, build more modern new classrooms and libraries that have air conditioning like the previous Labour Government did ( I think they did a great job on this!), so our kids can be kept safe from the 45 degree heat, and the tax payers can enjoy more benefits out of it.

***Big feet Charley:*** the infrastructure blueprint is sound when interest rates are at current lows, and the government may be able to get some return for some projects if it decides to privatize them in the future. I have always argued the country should come first ahead of politics. Every political party has its good policies. I think a good government has the ability to pick the best ideas, select the best people and be able to get its policies passed through the House and the Senate to get our country moving. The new budget is encouraging, addresses some hard issues and looks like moving in the right direction.

**All the best,**

**Charley Wang**

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***Notes & Disclosure:***

<sup>1</sup> 123 IGF and 123 IM staff own CSS share

<sup>2</sup> Images taken from 2014 October Analyst Presentation from CSS.

123 Investment Management Pty Ltd is the Investment Manager for **123 Investment and Growth Fund (123 IGF)**. Charley Wang is the CIO of 123 IGF, he has been working in the financial industry for over 20 years, including 15 years with Morgan Stanley Wealth Management (formerly Smith Barney Citigroup).

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