Sandon's Activist Approach Shakes Up Aussie Stocks -- Barron's Asia

By Daniel Shane

As an activist investor Gabriel Radzyminski loves bad companies. Underperforming Australian stocks are a magnet for the founder of Sandon Capital who wields the power of persuasion to convince management to make the hard changes needed to turnaround the fortunes of market laggards.

The strategy looks like it is working. The Sydney-based fund has returned more than 12% on average since inception in 2008 -- almost double the returns of Australian stocks. Similar to U.S. activist funds, Radzyminski looks for signs of shareholder discord at companies and leverages it to nudge changes in strategy or boot out underperforming and overpaid managers. He says it's these stocks that "are vulnerable to change."

On the face of it, Australia looks like fertile ground for activists as it offers a developed market in terms of corporate law and regulation but activist funds like Sandon Capital are thin on the ground. When the ex-Colonial First State analyst started the fund, he was told his ambitions "were futile." "They said no-one in Australia was interested and more importantly you wouldn't make any money out of it," he tells Barron's Asia. He reckons the challenges in the Australian market are cultural and there's a reluctance among shareholders to "rock the boat," as Radzyminski puts it. "We're suggesting to companies that what they're doing might not be the best thing for shareholders," he says, "and that's ultimately critical."

That Australian investors are sheepish when it comes to activism partly explains Sandon's modest size -- it manages about AUD60 million across a closed-end fund and the listed Sandon Capital Investments (ticker: SNC.AU). The funds are spread across 10 to 15 companies, while about 30% is kept in cash for any opportunities that may crop up. "From a fund-raising perspective it's quite challenging because people don't quite understand what you do," Radzyminski admits. "Anyone who invests might think they're an outlier. But we think being an outlier is a good thing."

Sandon Capital's philosophy is that activism is a natural evolution of traditional value investing. Like a value manager, Sandon screens for stocks that look under-valued by the market. But where they differ is that they don't hang around for the market to magically appreciate the latent value of a company's assets. Sandon, which is too small to have the clout to enact change itself, engages with other minority shareholders into backing its proposed action. "We're clearly punching above our weight in terms of the impact our shareholding can have," Radzyminski explains. "But we're firm believers in that if you've got a good idea you can leverage it beyond your own economic interest." A lot of this typically happens behind the scenes, but Sandon's not scared of duking it out in public either.

BlueScope Steel (BSL.AU) is arguably Sandon's most highly-publicized engagement. The fund manager last year released a lengthy report on the AUD2 billion miner, arguing it was the world's cheapest listed steel-maker. The argument was that BlueScope's assets in U.S. and Japanese joint ventures were alone worth more than Bluescope's market cap at the time. That implied the rump of the company's assets in Australia and New Zealand was worth nothing. Sandon said BlueScope was shipping about 500,000 tons in loss-making steel every year and it proposed mothballing the remaining blast furnace at its Port Kembla plant in New South Wales, doing away with its construction business and focusing on higher-end downstream products. Since then operating costs have been cut through lay-offs and pay freezes negotiated with unions, and profits have rebounded. Sure, BlueScope hasn't exactly done everything on Radzyminski's wish-list - not that he cares. The stock's up more than 80% since the Sandon report, even if a recent unexpected spike in steel prices has helped. "Activism is just a tool to enact change. We've almost doubled our money. The only thing that matters is we make money," he says. Radzyminski thinks BlueScope's share price has further upside.

A more recent focus for Sandon has been Tatts Group (TTS.AU). Radzyminski has urged the wagering and gaming giant to offload its sports betting business and concentrate on its real money-spinner -- lotteries. Radzyminski argues the lotteries business deserves a valuation similar to that of a listed infrastructure asset. Like a toll road, lottery operators are given lengthy concessions to run sweepstakes and they also draw reasonably predictable cash flows throughout the economic cycle. Sandon thinks Tatts is worth about AUD7.5 billion. Its current market cap is about AUD5.8 billion. Again, the activist firm's tiny stake in a blue chip like Tatts clearly limits its muscle, and Radzyminski is currently corralling other investors to get behind his thesis. "If there are aspects of what we're saying that they agree with, then they might start picking up the cudgels and making their views known to the company," he says.

Radzyminski's now digging for opportunities in companies that service Australia's beleaguered mining sector. Like the miners themselves, these stocks have been hammered by slumping commodity prices. The fact that one of Australia's top activists is sniffing around should have a few directors shifting in their seats uncomfortably.

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