

Coal Stocks Were Big Winners in 2021. A Value Investor Scooped Up More.

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Madrid-based Azvalor Asset Management increased its stake in coal miner Arch Resources, and retains a large investment in Consol Energy.
Luke Sharrett/Bloomberg

Shares of coal miner Arch Resources more than doubled in 2021, and a Spanish value investor sees more gains.

Madrid-based Azvalor Asset Management, which manages about \$2 billion in assets, acquired 292,902 more Arch (ticker: ARCH) shares to lift its stake to 1.06 million shares, a 6.9% stake, as of Jan. 10. Azvalor disclosed the larger stake in a form it filed with the Securities and Exchange Commission. According to S&P Capital IQ, that stake would make Azvalor the third-largest investor in Arch. Azvalor's last regulatory disclosure showed that it owned 766,257 Arch shares, a 5% stake, as of March 29, 2021.

Arch produces metallurgical coal, the type used to produce steel. Arch stock rocketed 109% in 2021, compared with a 27% rise in the S&P 500 index. The outperformance of the shares came in the first year of the Biden administration, which is aiming to wind down fossil fuels. Azvalor correctly saw upside in Arch and peer Consol Energy (CEIX) early in 2021, and disclosed positions in both.

Consol had an even better 2021 than Arch, with shares tripling in value. So far in 2022, Arch stock is up 5.7% while Consol stock has gained 8.9%; meanwhile, the index has slipped 2.2%.

"Arch offers a rare combination of operational excellence, shareholder-friendly capital allocation, and a very attractive valuation (three times normalized free-cash flow) not at all justified by the prospects we see for the business," wrote Azvalor founding partner, CEO, and co-Chief Investment Officer Álvaro Guzmán de Lázaro in an email. "We do not think it will take long for the market (maybe one or two quarters at the current crazy free-cash-flow generation) to correct this."

In October, Azvalor disclosed that it reduced the Consol investment by 688,050 shares to 3.2 million shares, a stake of 9.3%. Azvalor remains Consol's second-largest shareholder.

Guzmán de Lázaro noted that the sale of Consol shares was for regulatory purposes: under the EU's Undertakings for Collective Investment in Transferable Securities, or UCITS, directive, a single position can't exceed 10% of an investment fund's assets.

"With the rise of [Consol's] share price in October to above \$32, some of our vehicles had exceeded the 10% limit... and we profited from the October share-price spike to solve that situation (funds are granted a period to do that)," Guzmán de Lázaro wrote.

"Consol remains a top holding of ours...we still hold around 3 million shares or just above 8.5% of the capital," he added. Consol produces thermal coal, which is widely used for generating electricity. "The story is just 100% thermal here, so not as clear-cut as [metallurgical coal] at a first glance, but Consol's Northern Appalachian coal is the most efficient in the U.S., and the company trades under four times normalized free cash flow."

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