# BCI Minerals

## All on course

FY19, Q120 and DFS progress

Metals & mining

**In its September quarterly report, BCI reported that the definitive feasibility study (DFS) on the Mardie salt and potash project was 75% complete as at end-September 2019, with the expectation that it will be completed in Q1 CY20. In the meantime, the company is embarking on construction of a large-scale trial pond programme to test the envisaged materials and methods of construction and thereby substantially mitigate future construction risk.**

| Year end | Revenue (A$m) | PBT* (A$m) | EPS* (c) | DPS (c) | P/E (x) | Yield (%) |
|---|---|---|---|---|---|---|
| 06/18 | 33.0 | (16.9) | (4.3) | 0.0 | N/A | N/A |
| 06/19 | 54.2 | (4.6) | (0.8) | 0.0 | N/A | N/A |
| 06/20e | 85.8 | (12.7) | (3.2) | 0.0 | N/A | N/A |
| 06/21e | 55.2 | 2.8 | 0.3 | 0.0 | 58.8 | N/A |

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles and exceptional items.

## Approvals, funding and offtake initiatives advancing

At the same time as it is ramping up on-site activity at Mardie, BCI is also progressing its approvals, financing and offtake initiatives. Among other things, these include ongoing negotiations with the Northern Australia Infrastructure Facility (NAIF) to secure preferential debt funding and the signing of a number of additional memoranda of understanding (MoUs) with Asian chemical companies to sell 2.4Mtpa (60%) of Mardie's planned steady-state output of salt and 10ktpa (10%) of its planned steady-state output of SOP over a period of three years (cf 30% of its planned output of salt as at end-Q419). Finally, BCI expects to release its revised environmental review document (ERD) for public comment in Q4 CY19 with Australian Environmental Protection Authority endorsement targeted for Q2 CY20.

## Iron ore price continues to spur Iron Valley in Q1

In addition to updating the market on the progress of the Mardie DFS, BCI confirmed that the strong performance exhibited by its Iron Valley royalty asset at the end of FY19 continued into Q120. Iron Valley shipped 2.0Mt of iron ore in Q120, which resulted in record quarterly cash flow of A$10.7m, although BCI expects that provisionally priced September quarterly shipments will potentially attract a negative price finalisation adjustment of approximately A$3.0m in Q220. Nevertheless, BCI's September quarter EBITDA of A$7.7m is the second highest since operations began at Iron Valley in 2014 and compares with A$6.2m in Q419.

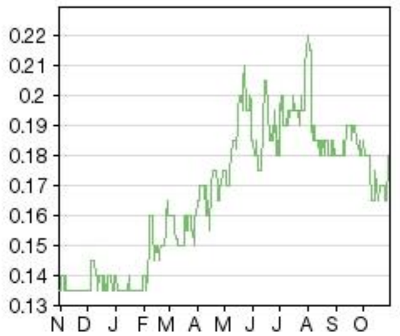
## Valuation: 2x share price, potentially 2.5x

In the wake of its announcement, we value BCI at 34.13c (cf 35.60 previously – although the decline in value may be entirely attributed to the lower BCI share price recently, which increases future assumed equity dilution for the development of Mardie). However, this valuation increases to as much as 44.38c if iron ore prices remain at current levels until the end of the life of operations at Iron Valley. Note that a further 2.43c should be added to all of these valuations to account for the value of BCI's Buckland iron ore assets.

**30 October 2019**

| | |
|---|---|
| **Price** | **A$0.18** |
| **Market cap** | **A$72m** |
| | A$1.4582/US$ |
| Net cash (A$m) at 30 September 2019 | 32.3 |
| Shares in issue | 397.6m |
| Free float | 63% |
| Code | BCI |
| Primary exchange | ASX |
| Secondary exchange | N/A |

### Share price performance




| % | 1m | 3m | 12m |
|---|---|---|---|
| Abs | 0.0 | (14.3) | 33.3 |
| Rel (local) | (0.4) | (13.5) | 13.2 |
| 52-week high/low | | A$0.22 | A$0.14 |

### Business description

BCI Minerals has two major assets in Western Australia, including a 100% interest in the Mardie salt and potash project and a royalty-type interest in the Iron Valley iron ore mine operated by Mineral Resources. It also has exploration tenements in iron ore and other minerals.

### Next events

| | |
|---|---|
| AGM | 27 November 2019 |
| Mardie DFS | Q1 CY20 |
| Mardie investment decision | Q1 CY20 |
| Q220 activities report | End January 2020 |

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## September quarterly update

BCI released its detailed results for FY19 on 25 October, albeit after having released a preliminary announcement on 23 August. Reported (ie un-normalised) pre-tax profits of A$11.4m were within 3.3% of our prior forecast (see our note Iron ore price continues to power ahead, published on 5 July 2019), while our cash estimate of A$34.0m was within 1.0% of the A$33.7m actually reported.

More significantly, in its September quarterly report (released on 28 October), BCI confirmed that the strong performance exhibited by its Iron Valley royalty asset at the end of FY19 continued into Q120. Iron Valley shipped 2.0Mt of iron ore in Q120 (c 65% fines), which resulted in record quarterly cash flow of A$10.7m during the period, although BCI expects that provisionally priced September quarterly shipments will potentially attract a negative price finalisation adjustment of approximately A$3.0m to be realised in the December quarter (and payable in January 2020) given the decline in iron ore prices since July. Nevertheless, BCI's September quarter EBITDA of A$7.7m is reported to be the second highest on record since operations at Iron Valley commenced in 2014 and compares with A$6.2m in Q419 (including a positive A$1.4m prior quarter adjustment) from 1.9Mt of shipments.

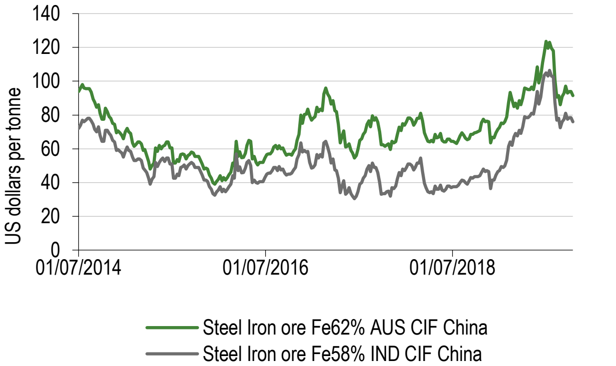
Although the price of 58% CFR iron ore (a close proxy to the price received by Iron Valley for its product) has declined by c 29% since its peak of US$106.5/t in mid-July, it has since stabilised and traded within a relatively narrow range of US$77.25/t ±US$4.75/t, with the result that it is tracking relatively close to Edison's prior expectations for FY20:

**Exhibit 1: Price of standard grade 58% CFR iron ore, July 2014 to July 2020e**


Source: Refinitiv, Edison Investment Research

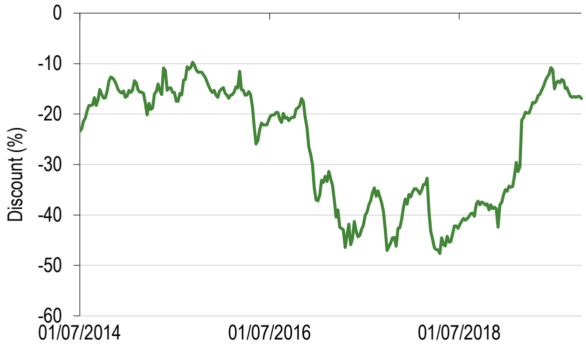
Despite the well-documented price falls of both 58% and 62% iron ore, the price of the former has apparently stabilised at an historically modest discount relative to the latter – more akin to market conditions before May 2016 than those experienced during the period between November 2016 and January 2019, prior to Vale's Brumadinho tailings dam disaster:

**Exhibit 2: 62% iron ore price (US$/t) and 58% iron ore price, July 2014 to present**




Source: Refinitiv

**Exhibit 3: Discount of 58% iron ore price to 62% iron ore price, July 2014 to present (%)**




Source: Edison (underlying data: Refinitiv)

At the same time, the operator of the Iron Valley mine, Mineral Resources, has also completed its annual update of Iron Valley mineral resources and ore reserves and determined that (at 30 June 2019) both are almost exactly in line with those that would be expected after allowing for one year's worth of mining depletion from the resources and reserves reported in June 2018.

As a result, we are leaving our earnings forecasts for FY20 and subsequent years ostensibly unchanged for the moment (with the exception of adjusting for forex and the share price, which affects future assumed equity dilution for the development of Mardie).

## Mardie update

A DFS on the Mardie salt and potash project is underway and was reported by BCI to be 75% complete as of end-September 2019, with the expectation that it will be completed in Q1 CY20. Salient features of progress made during the September quarter are summarised below:

- Design of key salt and sulphate of potash (SOP) production infrastructure (including the ponds, crystallisers and processing plants) has been completed, or is nearing completion, and the focus is shifting towards development of the DFS production ramp-up schedules, capital and operating cost estimates.
- Refinements to the project layout have been completed and detailed designs concluded. A trade-off study relating to the configuration of the port has confirmed the optimal length of the jetty to be 3.1km (cf 7km previously) to maximise the cost benefit between the jetty length and related dredging requirements. The difference will be made up by a 3.5km causeway incorporating both a road and a conveyor belt, while the salt stockpile will be relocated from the plant to the shoreline.
- Marine geotechnical drilling has been completed.
- The 1:40,000 small-scale trial ponds have been fully constructed and the first raw salt samples crystallised and harvested to be tested for quality and purity. The trial will provide site-specific evaporation data at a range of densities and simulate the full evaporation process at a reduced scale. Similar samples for SOP (which crystallises later in the process) will follow in due course.
- In addition to its small-scale evaporation trials, BCI is planning to undertake (and has received environmental approval for) a large-scale trial pond programme that will include construction of a 32ha trial pond (including 2.3km of pond walls and the final seawalls for the project's Pond 1), a seawater intake facility incorporating one of the proposed six operating pumps, supporting infrastructure, roads and a 36-bed accommodation village. The principal rationale of the large-

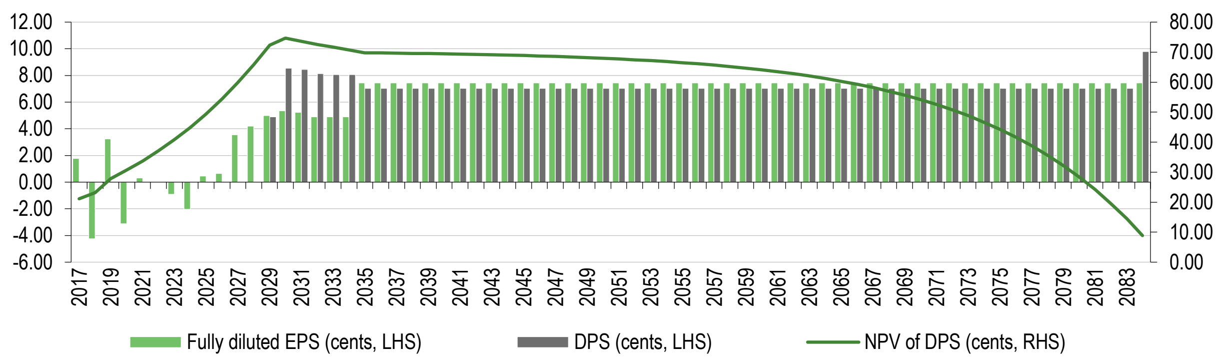
scale pond trial is to test the envisaged method of constructing the evaporation pond wall and the materials involved (especially the construction time available per day in the inter-tidal area), thereby substantially mitigating future construction risk. In addition, it will validate the permeability of the underlying clay soils over a large area, validate evaporation assumptions over a large area and validate pump rates and capabilities. Design work for the large-scale ponds has now been completed and construction is due to commence imminently at a total expected cost of A$15m – although note that this was already included in our financial forecasts for FY20.

- BCI submitted a draft environmental review document (ERD) for the Mardie project to the Western Australian Environmental Protection Authority (EPA) in April 2019. Since then, it has revised the draft to incorporate refinements to the project layout and feedback from the EPA and other government departments and agencies and now expects to release the document for public comment in Q4 CY19 with EPA endorsement targeted for Q2 CY20.
- Additional memoranda of understanding (MoUs) were agreed with Asian chemical companies and traders during the quarter. As a result, BCI now has six MoUs that cover 2.4Mtpa (60%) of Mardie's planned steady-state salt output and 10ktpa (10%) of its planned steady-state SOP output over a period of three years. This compares with MoUs covering 30% of Mardie's planned steady-state salt production over three years at the end of the June quarter. Note that BCI reports that positive discussions are ongoing with a number of other salt and SOP end-users and traders and that BCI is aiming to secure additional salt MoUs by the end of the calendar year.
- Finally, in respect of funding, securing long tenor debt is an important part of Mardie's strategy, to which end it is progressing discussions with the Federal Government's Northern Australia Infrastructure Facility (NAIF). It has also started engaging with commercial banks for the provision of project finance debt to complement any NAIF debt facilities.

## Valuation and sensitivities

As stated previously, the only other of our assumptions to change are BCI's share price (which has fallen from 19.5c at the time of our last note to 18c currently) and the A$/US$ rate (which has fallen to A$1.4582/US$). The remainder of our assumptions remain unchanged with the result that our long-term estimates of BCI's earnings, (maximum potential) dividends per share and valuation trajectory are also substantially unchanged as follows:

**Exhibit 4: BCI EPS and (maximum potential) DPS forecasts, FY18–83e (cents)**




Source: Edison Investment Research. Note: Income derived from Iron Valley and Mardie, combined; no contribution assumed from Buckland or any other assets.

Discounting at our customary discount rate of 10% per year, the (fully diluted) value of these cash flows to shareholders is 34.13 Australian cents at 1 July 2019. This compares with a valuation of 35.60c previously although the reduction may be entirely attributed to the recent decline in BCI's share price (which increases future assumed equity dilution). If the share price was unchanged, the updated valuation of BCI would instead be 36.13c.

To this should then be added a further 2.43c for BCI's Buckland iron ore assets to take the total to 36.56c.

## Sensitivities

All other things being equal, our earnings forecasts will be affected by the extent to which iron ore prices either remain at current levels or decline as shown in Exhibit 1. As can be seen in Exhibit 5, we calculate that, if iron ore prices remain at current levels (58% CFR at US$76/t) and all other things remain equal, BCI's valuation will rise by 14.0%, from 34.13c/share to 38.91c/share. Alternatively, if the company takes the opportunity to reduce future equity funding as a result of a higher iron ore price, the valuation instead increases by 30.0% to 44.38c/share:

**Exhibit 5: BCI Minerals valuation sensitivity to future Iron Valley iron ore pricing scenarios**

| Scenario | Valuation (Australian cents per share) | Incremental change (cps) | Incremental change (%) | Maximum net debt funding requirement (A$m) | Maximum leverage* (%) |
|---|---|---|---|---|---|
| Base case | 34.13 | | | 272.2 | 50.0 |
| Iron ore price remains at current level until end of life of mine | 38.91 | +4.78 | +14.0 | 217.8 | 39.8 |
| Ditto with reduced future equity funding requirement | 44.38 | +10.25 | +30.0 | 273.7 | 50.0 |

Source: Edison Investment Research. Note: *Defined as (net debt)/(net debt+equity).

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**Exhibit 6: Financial summary**

| A$'000s | 2015 | 2016 | 2017 | 2018 | 2019 | 2020e | 2021e |
|---|---|---|---|---|---|---|---|
| June | IFRS | IFRS | IFRS | IFRS | IFRS | IFRS | IFRS |
| **PROFIT & LOSS** | | | | | | | |
| Revenue | 281,211 | 151,279 | 64,324 | 33,029 | 54,170 | 85,774 | 55,225 |
| Cost of Sales | (278,465) | (158,210) | (55,190) | (47,442) | (56,781) | (96,404) | (50,022) |
| Gross Profit | 2,746 | (6,931) | 9,134 | (14,413) | (2,611) | (10,630) | 5,203 |
| EBITDA | 2,746 | (6,931) | 9,134 | (14,413) | (2,611) | (10,630) | 5,203 |
| Operating Profit (before amort. and except.) | (26,090) | (12,622) | 5,665 | (17,330) | (5,234) | (13,253) | 2,580 |
| Intangible Amortisation | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Exceptionals | (170,881) | (40,108) | (302) | 0 | 15,991 | 0 | 0 |
| Other | (2,935) | 812 | (5) | 0 | 0 | 0 | 0 |
| Operating Profit | (199,906) | (51,918) | 5,358 | (17,330) | 10,757 | (13,253) | 2,580 |
| Net Interest | (3,505) | (951) | 311 | 420 | 630 | 506 | 254 |
| Profit Before Tax (norm) | (29,595) | (13,573) | 5,976 | (16,910) | (4,604) | (12,748) | 2,834 |
| Profit Before Tax (FRS 3) | (203,411) | (52,869) | 5,669 | (16,910) | 11,387 | (12,748) | 2,834 |
| Tax | 44,912 | (27,086) | 0 | 0 | 1,510 | 0 | 0 |
| Profit After Tax (norm) | 12,382 | (39,847) | 5,971 | (16,910) | (3,094) | (12,748) | 2,834 |
| Profit After Tax (FRS 3) | (158,499) | (79,955) | 5,669 | (16,910) | 12,897 | (12,748) | 2,834 |
| Average Number of Shares Outstanding (m) | 174.8 | 196.2 | 316.7 | 394.6 | 397.2 | 397.6 | 925.7 |
| EPS - normalised (c) | 7.1 | (20.3) | 1.9 | (4.3) | (0.8) | (3.2) | 0.3 |
| EPS - normalised and fully diluted (c) | 7.1 | (19.5) | 1.9 | (4.3) | (0.8) | (3.1) | 0.3 |
| EPS - (IFRS) (c) | (90.7) | (40.8) | 1.8 | (4.3) | 3.2 | (3.2) | 0.3 |
| Dividend per share (p) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Gross Margin (%) | 1.0 | -4.6 | 14.2 | -43.6 | -4.8 | -12.4 | 9.4 |
| EBITDA Margin (%) | 1.0 | -4.6 | 14.2 | -43.6 | -4.8 | -12.4 | 9.4 |
| Operating Margin (before GW and except.) (%) | -9.3 | -8.3 | 8.8 | -52.5 | -9.7 | -15.5 | 4.7 |
| **BALANCE SHEET** | | | | | | | |
| Fixed Assets | 154,904 | 86,546 | 78,059 | 85,768 | 74,075 | 81,452 | 184,389 |
| Intangible Assets | 60,237 | 33,618 | 33,063 | 43,615 | 34,392 | 44,392 | 40,392 |
| Tangible Assets | 94,667 | 52,928 | 44,996 | 42,153 | 39,683 | 37,060 | 143,997 |
| Investments | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Current Assets | 102,374 | 23,204 | 46,429 | 20,270 | 56,293 | 35,436 | 109,747 |
| Stocks | 9,886 | 61 | 0 | 0 | 0 | 117 | 76 |
| Debtors | 24,427 | 13,694 | 10,053 | 7,213 | 22,251 | 18,068 | 13,617 |
| Cash | 67,671 | 9,449 | 36,376 | 13,057 | 33,702 | 16,911 | 95,715 |
| Other | 390 | 0 | 0 | 0 | 340 | 340 | 340 |
| Current Liabilities | (77,222) | (21,769) | (12,107) | (9,373) | (18,092) | (17,360) | (11,151) |
| Creditors | (70,947) | (19,749) | (12,107) | (9,373) | (18,092) | (17,360) | (11,151) |
| Short term borrowings | (6,275) | (2,020) | 0 | 0 | 0 | 0 | 0 |
| Long Term Liabilities | (20,773) | (11,307) | (5,225) | (6,054) | (8,664) | (8,664) | (8,664) |
| Long term borrowings | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other long term liabilities | (20,773) | (11,307) | (5,225) | (6,054) | (8,664) | (8,664) | (8,664) |
| Net Assets | 159,283 | 76,674 | 107,156 | 90,611 | 103,612 | 90,864 | 274,321 |
| **CASH FLOW** | | | | | | | |
| Operating Cash Flow | (77,686) | (19,721) | 11,860 | (11,957) | (7,663) | (7,297) | 3,487 |
| Net Interest | (1,120) | 0 | 0 | 0 | 0 | 506 | 254 |
| Tax | 44,912 | (27,086) | 0 | 0 | 1,510 | 0 | 0 |
| Capex | (10,987) | (8,075) | (2,220) | (10,074) | (496) | (10,000) | (109,560) |
| Acquisitions/disposals | 24,338 | 0 | (5,151) | (1,288) | 27,294 | 0 | 4,000 |
| Financing | 6,118 | 1,510 | 24,403 | 0 | 0 | 0 | 180,623 |
| Dividends | (18,652) | 0 | 0 | 0 | 0 | 0 | 0 |
| Net Cash Flow | (33,077) | (53,372) | 28,892 | (23,319) | 20,645 | (16,791) | 78,804 |
| Opening net debt/(cash) | (94,473) | (61,396) | (7,429) | (36,376) | (13,057) | (33,702) | (16,911) |
| HP finance leases initiated | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other | 0 | (595) | 55 | 0 | 0 | 0 | 0 |
| Closing net debt/(cash) | (61,396) | (7,429) | (36,376) | (13,057) | (33,702) | (16,911) | (95,715) |

Source: Company sources, Edison Investment Research

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