BCI Minerals

Resilient iron ore price buoys Q220

Quarterly update

Metals & mining

In its December quarterly report, BCI Minerals confirmed that the strong performance exhibited by its Iron Valley royalty asset in Q120 continued into Q220. Iron Valley shipped 1.5Mt of iron ore in Q220 (cf 2.0Mt in Q120), comprising 60% fines (cf 65%), resulting in a quarterly EBITDA of A$3.2m, including a negative prior quarterly adjustment of A$1.6m (cf a near record quarterly EBITDA of A$7.7m in Q120). Notwithstanding the adjustment, BCI's Q220 EBITDA of A$3.2m was nevertheless higher than any other quarter since Q317 except Q419 and Q120.

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	87.1	(12.5)	(3.1)	0.0	N/A	N/A
06/21e	56.1	3.0	0.3	0.0	54.4	N/A

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

Major share price catalyst in the form of Mardie DFS

The timetable surrounding Mardie has slipped by an immaterial one quarter, with the DFS now expected in Q2 CY20 (from Q1 CY20 previously) and a final investment decision in Q3 CY20. More significantly, in our report Gold stars and Black holes: Analysing the discount: From resource to sanction, published in January 2019, we observed that, excluding outliers, the average valuation of companies with projects at PFS stage is 9.9% of attributable NPV. On this basis (and assuming a post-tax NPV of 70% of pre-tax NPV of A$560m), an average valuation for Mardie currently would be A$38.8m, or 9.76 Australian cents per share (ie 29% of our current BCI valuation – see below). However, if the DFS on Mardie, which is underway, is completed on approximately the same terms as the optimised PFS, we would expect this valuation to increase approximately threefold, to c 30.9% of NPV, or 28.34c per BCI share (ie 1.7x BCI's current share price) for Mardie alone, excluding BCI's other assets such as Iron Valley, Buckland.

Salt price simultaneously on the rise

As BCI is progressing its DFS, it also reports that for the 10 months to October 2019, international trade data confirms that the average value of Australian salt exported to Asia has risen by 20% compared to the 2018 average price.

Valuation: 2x share price, potentially 2.8x

Since our last note, we have adjusted our valuation solely for changes in the share price (which affects future assumed dilution) and the US$/A$ forex rate, with the result that our updated valuation per BCI share remains largely unchanged at 33.75c (cf 34.13 previously). However, this valuation increases to as much as 45.82c (44.38c previously) if the iron ore price remains at current levels. 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.

31 January 2020

Price	**A$0.17**
Market cap	**A$68m**
	A$1.4805/US$
Net cash (A$m) at 31 December 2019	34.0
Shares in issue	397.6m
Free float	63%
Code	BCI
Primary exchange	ASX
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(2.9)	(5.7)	22.2
Rel (local)	(5.5)	(9.9)	2.3
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.

Next events

Mardie DFS	Q2 CY20
Large-scale trial pond construction	Q2 CY20
Mardie investment decision	Q3 CY20
Mardie project construction	Early 2021

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Edison profile page

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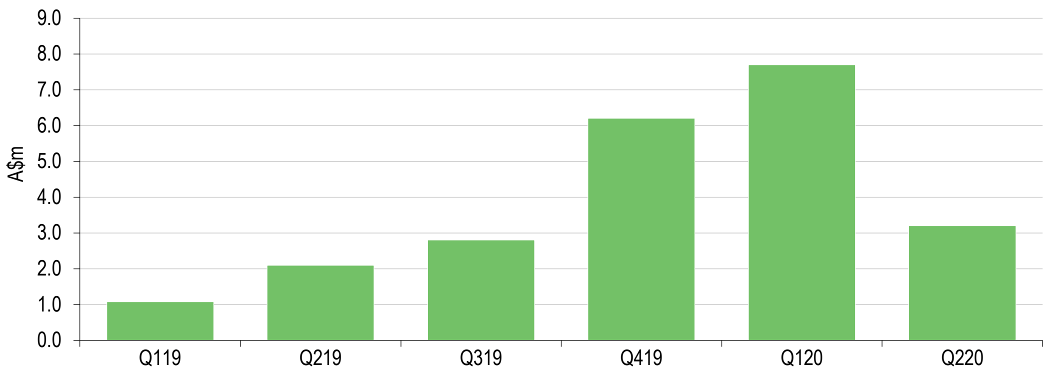
Iron Valley quarterly update

In its December quarterly report (released on 24 January), BCI confirmed that the strong performance exhibited by its Iron Valley royalty asset in Q120 continued into Q220. Iron Valley shipped 1.5Mt of iron ore in Q220 (cf 2.0Mt in Q120), comprising 60% fines (cf 65% in Q120), resulting in quarterly EBITDA of A$3.2m, including a negative prior quarterly adjustment of A$1.6m. This compared with a record quarterly cash flow of A$10.7m in Q120, albeit with the expectation of a negative price finalisation adjustment of approximately A$3.0m to be realised in Q220 (for EBITDA of A$7.7m). Notwithstanding the prior quarterly adjustment, BCI's December's quarter EBITDA of A$3.2m was nevertheless higher than at any other time since Q317, with the sole exceptions of Q419 and Q120.

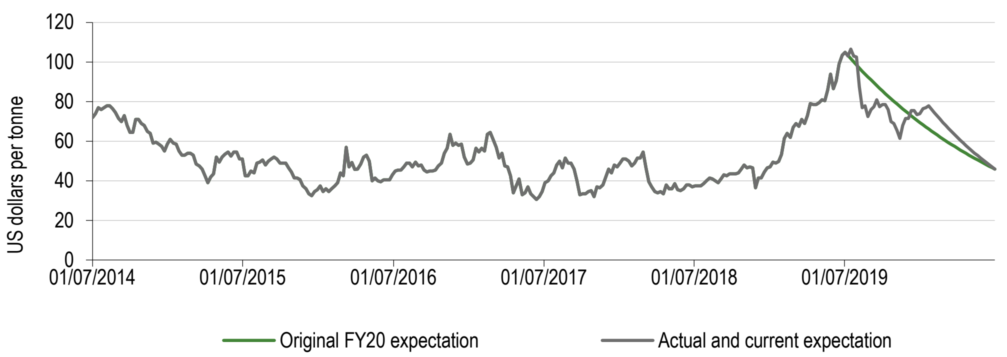
Exhibit 1: Iron Valley quarterly EBITDA attributable to BCI (A$m)



Source: BCI Minerals.

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 27% since its peak of US$106.5/t in mid-July 2019, it has since stabilised and traded generally within the range US$74/t ±US$4/t, with the result that (on average) it is tracking relatively close to Edison's original expectation for FY20 (see our note, BCI Minerals: Iron ore price continues to power ahead, published on 5 July 2019). On current trends therefore (the grey line in Exhibit 2 below) the average price of 58% CFR iron ore for BCI's FY20 will be US$71.02/t, compared with an original expectation (the green line) of an average price of US$71.53/t:

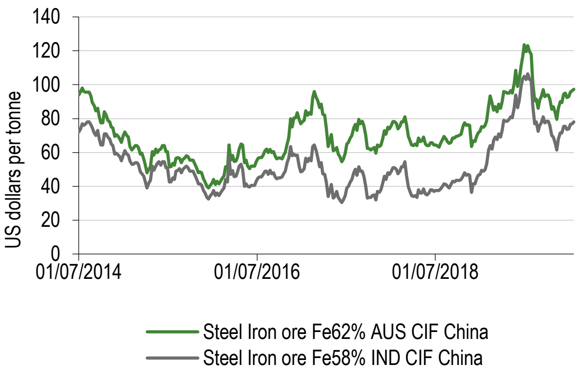
Exhibit 2: Price of standard grade 58% CFR iron ore, July 2014 to July 2020e



Source: Refinitiv, Edison Investment Research

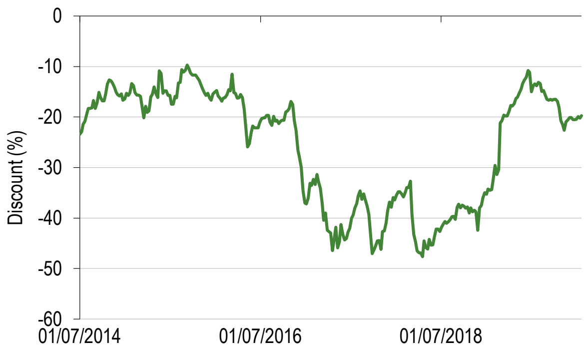
Moreover, despite the well-documented price falls of both 58% and 62% iron ore, the price of the former has apparently stabilised at a historically modest discount relative to the latter – more akin to market conditions before November 2016 than those experienced during the period between November 2016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

Exhibit 3: 62% iron ore price (US$/t) and 58% iron ore price, July 2014 to present



Source: Refinitiv

Exhibit 4: Discount of 58% iron ore price to 62% iron ore price, July 2014 to present (%)



Source: Edison Investment Research (underlying data: Refinitiv)

As a result, we are leaving our earnings forecasts for FY20 and subsequent years substantially unchanged (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 definitive feasibility study (DFS) on the Mardie salt and potash project is underway and is expected to be completed in Q2 CY20. Salient features of progress made during the December quarter are summarised below:

- Design and engineering of all key salt and sulphate of potash (SOP) production, port and support infrastructure has been completed as well as production ramp-up schedules. As a result, preliminary capital and operating cost estimates are being compiled and validated at the same time as a value engineering process is underway to optimise designs and reduce capex and opex, which is expected to be completed by end-Q1 CY20.
- BCI is conducting evaporation trials at the Mardie site, comprising 21 pan evaporators plus a 1:40,000 scale version of the entire future pond and crystalliser configuration. The 1:40,000 small-scale trial ponds have been fully constructed and are now operating at steady-state, providing samples for test work and marketing.
- 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 c A$12m (A$15m including camp that has already been built), 32ha trial pond (including 2.3km of pond walls, some of which are final seawalls for the project's Pond 1) and a seawater intake facility incorporating one of the proposed six operating pumps. The principal rationale of the large-scale pond trial is to test the envisaged method of constructing the evaporation pond walls 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 and construction of a 36-bed accommodation village has been completed and construction of the trial pond itself is due to commence in Q2 CY20 after the end of the wet season.
- 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

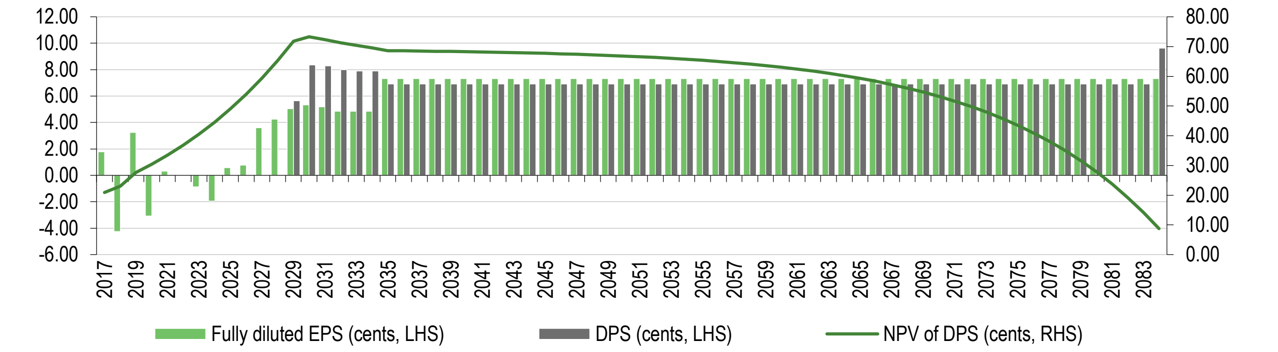
revised the draft to incorporate improvements to the project layout and feedback from the EPA and other government departments and agencies. The final ERD is expected to be submitted in the current quarter (Q1 CY20) and released for public comment in Q2 CY20 (cf Q4 CY19 previously) with EPA endorsement targeted for H2 CY20 (cf Q2 CY20 previously).

- Mining Lease applications (together with their supporting Mining Proposal and Mine Closure Plan documents) were submitted to the regulator during the quarter under review and are expected to be granted by Q3 CY20.
- The port land and marine areas required for the project were identified with the Pilbara Ports Authority (PPA) during 2019 and the Department of Planning, Lands & Heritage is expected to formally secure tenure during 2020. At the same time, a non-binding term sheet has been executed with the PPA, setting out the key principles, process and timeline for the finalisation of the Mardie Port lease documentation, which is currently being drafted and reviewed.
- Additional memoranda of understanding (MoUs) were agreed with Asian chemical companies and traders during the quarter. As a result, BCI now has 10 MoUs (vs six previously) that cover 2.8Mtpa, or 70% (cf 2.4Mtpa and 60%) of Mardie's planned steady-state salt output and two MoUs (vs one previously) that cover 80ktpa, or 80% (cf 10ktpa and 10%), of its planned steady-state SOP output over a period of three years. 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 in the coming months.
- Finally, in respect of funding, securing long tenor debt is an important part of Mardie's strategy, to which end it is progressing through the Due Diligence Stage (the third of four stages) of the Federal Government's Northern Australia Infrastructure Facility (NAIF) assessment process. It is also advancing discussions and indicative term sheets with Australian and international commercial banks for the provision of project finance debt to complement any NAIF debt facilities.

Valuation

As stated previously, the only assumptions to change in our valuation are BCI's share price (which has fallen fractionally from 18c at the time of our last note to 17c currently) and the A$/US$ rate (which has weakened from A$1.4582/US$ to A$1.4805/US$). 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 5: BCI EPS and (maximum potential) DPS forecasts, FY18–84e (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 33.75 Australian cents (cf 34.13c previously). To this should then be added a further 2.43c for BCI's Buckland iron ore assets to take the total to 36.18c.

Sensitivities

All other things being equal, our near-term earnings forecasts in particular will be affected by the extent to which iron ore prices either remain at current levels or decline as shown in Exhibit 2. As can be seen in Exhibit 6, we calculate that, if iron ore prices remain at current levels (58% CFR at US$78/t) and all other things remain equal, BCI's valuation will rise by 15.5%, from 33.75c/share to 38.98c/share. In addition, 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 35.8% to 45.82c/share:

Exhibit 6: BCI Minerals valuation sensitivity to future Iron Valley iron ore pricing scenarios

Scenario	Valuation (Australian cents per share)	Incremental change (c/share)	Incremental change (%)	Maximum net debt funding requirement (A$m)	Maximum leverage* (%)
Base case	33.75			271.4	49.9
Iron ore price remains at current level until end of life of mine	38.98	+5.23	+15.5	209.8	38.3
Ditto with reduced future equity funding requirement	45.82	+12.07	+35.8	273.9	50.0

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

Financials

BCI's cash flow is necessarily somewhat lumpy. Its September 2019 quarter net receipts of A$10.7m, for example, were received in October 2019 and its December quarter net receipts of A$1.5m will be received by the end of January 2020, reflecting provisional December quarter net receipts less total finalisation adjustments relating to the September quarter. Nevertheless, the robust performance exhibited by Iron Valley so far is FY20 is acting to substantially defray the ongoing costs of Mardie DFS and early development costs, as demonstrated by the cash balances declared by the company in recent months (below):

Exhibit 7: BCI recently reported net cash, December 2018 to December 2019

Date	End-Dec 2018	End-Mar 2019	End-May 2019	End-Jun 2019	End-Sept 2019	End-Nov 2019	End-Dec 2019
BCI net cash (A$m)	36.6	35.4	34.8	33.7	32.3	37.3	34.0
Net cash per BCI share (cents)	9.3	8.9	8.8	8.5	8.1	9.4	8.6

Source: BCI Minerals.

We expect BCI's net cash position to reduce quite materially in H2FY20, in particular under the capex influence of the construction of the large-scale trial pond. Nevertheless, at this time, we forecast it to remain at a healthy A$20.1m as at end-June 2020, prior to BCI making a final investment decision on the Mardie project in Q3 CY20 (see Exhibit 8, below).

Exhibit 8: 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	87,086	56,069
Cost of Sales	(278,465)	(158,210)	(55,190)	(47,442)	(56,781)	(97,481)	(50,713)
Gross Profit	2,746	(6,931)	9,134	(14,413)	(2,611)	(10,395)	5,356
EBITDA	2,746	(6,931)	9,134	(14,413)	(2,611)	(10,395)	5,356
Operating Profit (before amort. and except.)	(26,090)	(12,622)	5,665	(17,330)	(5,234)	(13,018)	2,733
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	(13,018)	2,733
Net Interest	(3,505)	(951)	311	420	630	506	302
Profit Before Tax (norm)	(29,595)	(13,573)	5,976	(16,910)	(4,604)	(12,513)	3,035
Profit Before Tax (FRS 3)	(203,411)	(52,869)	5,669	(16,910)	11,387	(12,513)	3,035
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)	(12,513)	3,035
Profit After Tax (FRS 3)	(158,499)	(79,955)	5,669	(16,910)	12,897	(12,513)	3,035
Average Number of Shares Outstanding (m)	174.8	196.2	316.7	394.6	397.2	397.6	956.8
EPS - normalised (c)	7.1	(20.3)	1.9	(4.3)	(0.8)	(3.1)	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	(3.1)	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	-11.9	9.6
EBITDA Margin (%)	1.0	-4.6	14.2	-43.6	-4.8	-11.9	9.6
Operating Margin (before GW and except.) (%)	-9.3	-8.3	8.8	-52.5	-9.7	-14.9	4.9
BALANCE SHEET							
Fixed Assets	154,904	86,546	78,059	85,768	74,075	78,452	184,389
Intangible Assets	60,237	33,618	33,063	43,615	34,392	41,392	37,392
Tangible Assets	94,667	52,928	44,996	42,153	39,683	37,060	146,997
Investments	0	0	0	0	0	0	0
Current Assets	102,374	23,204	46,429	20,270	56,293	38,937	110,354
Stocks	9,886	61	0	0	0	119	77
Debtors	24,427	13,694	10,053	7,213	22,251	18,344	13,825
Cash	67,671	9,449	36,376	13,057	33,702	20,133	96,112
Other	390	0	0	0	340	340	340
Current Liabilities	(77,222)	(21,769)	(12,107)	(9,373)	(18,092)	(17,625)	(11,322)
Creditors	(70,947)	(19,749)	(12,107)	(9,373)	(18,092)	(17,625)	(11,322)
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	91,099	274,758
CASH FLOW							
Operating Cash Flow	(77,686)	(19,721)	11,860	(11,957)	(7,663)	(7,074)	3,614
Net Interest	(1,120)	0	0	0	0	506	302
Tax	44,912	(27,086)	0	0	1,510	0	0
Capex	(10,987)	(8,075)	(2,220)	(10,074)	(496)	(7,000)	(112,560)
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	(13,569)	75,979
Opening net debt/(cash)	(94,473)	(61,396)	(7,429)	(36,376)	(13,057)	(33,702)	(20,133)
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)	(20,133)	(96,112)

Source: Company sources, Edison Investment Research

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