

BCI Minerals (BCI)

Iron ore and NAIF at the party

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KEY POINTS

BCI's delivered record EBITDA from Iron Valley in 2Q21 (\$10m). We see four material drivers for BCI in terms of iron ore earnings in the near to medium term:

- 3Q21 average iron ore benchmark pricing to date is A\$217/t, vs. A\$172/t in 1H21 (up 26%), noting that EBITDA % gains are higher than revenue gains for BCI;
- Volumes shipped from Iron Valley are expected to be higher in 2H21 vs. 1H21. Guidance implies 4.6mt 2H21 vs. 2.9mt 1H21;
- BCI receives a royalty payment for iron ore shipped from Iron Valley that increases as the A\$ iron ore price increases. We expect a higher royalty rate on a higher price will lift 3Q21 EBITDA; and
- BCI agreed to a \$25m EBITDA reduction in royalties to help fund a mine cut back (starting FY21). We expect this will be repaid in late FY21, lifting EBITDA in FY22.

As good as iron ore is to BCI, the Mardie salt project is the main game. Last month, BCI secured up to \$450m of 15-year debt funding from NAIF. This funding facility is larger than we had factored in. In our opinion, this materially de-risks the ability of BCI to fund the project. As the share price barely moved, we believe that the market has missed this major catalyst.

The remaining major hurdle is environmental approvals, expected to be in place in 2Q21 (not far away). In our experience, stocks that appear funded and have approvals re-rate. With the general re-rate of commodity stocks and with likely upcoming catalysts, BCI looks poised to re-rate in the near term.

Compass Minerals is BCI's closest peer. For FY21, it is trading at 9.1x EV/EBITDA, highlighting the potential value of Mardie outside of takeover, implying a long-term valuation of \$1.8bn (9x the current market cap, plus BCI has \$79m cash and no debt).

We have lifted our iron ore price forecasts and the royalty rate received by BCI. This increases our forecasts by \$18m / \$18m and \$13m respectively between FY21-FY23. Whilst this is a material increase, risk is probably still to the upside, unless iron ore prices materially decline.

INVESTMENT VIEW

Due to the long lead time to reach steady state production (FY28), we use DCF to value BCI. Due to the NAIF funding package, we lower our equity risk discount to 20% (from 25%). The higher forecasts result in an un-risked valuation of \$0.67/share (from \$0.61). Applying a 20% risk discount results in a price target of \$0.53/share (from \$0.46), ~80% above the current share price. We retain our Speculative Buy recommendation.

Relative to ASX listed SOP peers, BCI looks materially undervalued. We expect it has high near-term re-rating potential and should attract investors looking for immediate share price growth due to pending catalysts. Longer term, BCI is forecast to generate ~\$200m pa of EBITDA. With a very long project life, an endless resource and strong ESG elements to the Mardie salt project, it should be on the radar.

Whilst a large capital raising is coming, there is likely to be a rights component and the share price could well be a lot higher post achieving environmental approvals. We recommend accumulating a position now.

Recommendation Speculative BUY

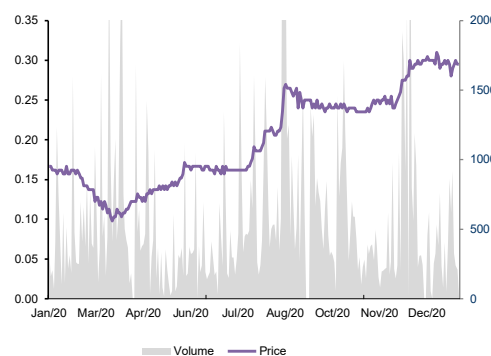
Previous Recommendation	Spec. Buy \$0.46
Risk Rating	High
Current Share Price	\$0.295
12 Month Price Target	\$0.53/share
Price target Methodology	DCF
Total Return (Capital + Yield)	80%
Mardie steady state EBITDA	\$200m pa
Market Capitalisation	\$177m
Liquidity	\$0.1m/day

Financial Forecasts & Valuation Metrics

BCI Y/E Jun A\$m	FY20A	FY21F	FY22F	FY23F
Revenue	54.2	101.8	85.7	72.7
EBITDA	16.4	11.7	13.9	7.7
EPS Adj (c)	4.4	1.8	0.6	0.1
EPS Growth	243%	60%	67%	-79%
DPS (c)	0.0	0.0	0.0	0.0
Yield (%)	0.0%	0.0%	0.0%	0.0%
EV/EBITDA (x)	6.0	(16.9)	(1.5)	26.8
PE Underlying (x)	5.3	13.1	40.2	190.6
Gearing (%)	-66%	-555%	-65%	14%

Source: PAC Partners estimates

12 Month Share Price and Volume



Key Milestones

- Achieving environmental approval, expected Q2 2021
- Achieving FID, expected in late Q2 2021
- General re-rate occurring in commodity stocks
- Further trial work and optimisation studies reducing the risk of cost overruns
- Re-rating as the prospect of Mardie gets factored in

DISCLOSURE: Entities associated with the author of this report own shares in BCI Minerals Limited

The information contained in this report is provided by PAC Partners to Wholesale Investors only.

The information contained in this report is to be read in conjunction with other important disclosures at the end of this document.

2Q FY21 Update

Iron Valley appears to be a solid cash generator for several years to come

The iron ore price is hovering around all-time highs. Any supply response appears small in the near-term

3Q21 Iron Valley EBITDA are leveraged, with several factors assisting

NAIF's funding of the project (subject to conditions) was expected to be a major catalyst. As investors start to appreciate the project is very likely to occur, BCI should re-rate

IRON ORE PRICE DRIVING EARNINGS

2Q21 shipments from Iron Valley were 1.6mt for the quarter (2.9mt 1H21). Guidance for iron ore shipments via Utah Point from MIN (the operator of Iron Valley) is 7.5 – 8.5mt. Some of this amount shipped could come from other mines, we estimate guidance is for 7.5mt from Iron Valley. This leaves 4.6mt to be shipped in 2H21. Whilst this is a big step up in volume, our understanding is that volumes were always going to be 2H weighted due to equipment being diverted to undertake a large cut back in the 1H21.

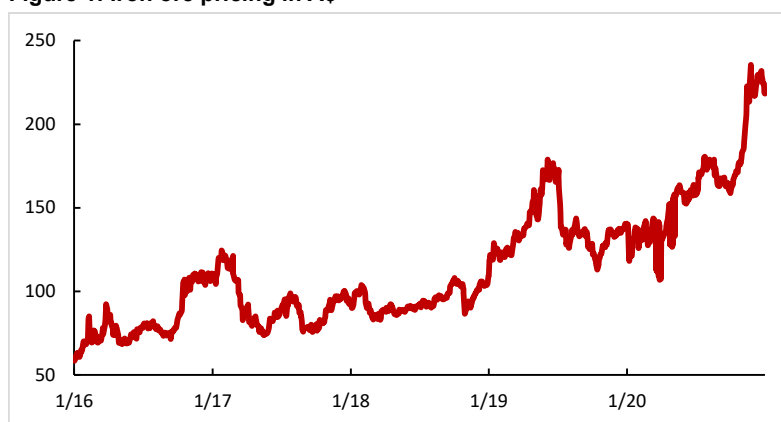
BCI indicated that in 2Q21, Iron Valley generated record EBITDA of \$10m (\$17.1m 1H21). This is after allowing a 40% reduction in EBITDA agreed to fund the large cutback. We estimate that BCI has now funded \$11.3m of the \$25m cutback funding and are likely to revert to the full fee structure from Iron Valley in either late FY21 or early FY22.

BCI's royalty rate is on a sliding scale, the higher the iron ore price, the higher the royalty rate. We expect BCI to access a higher royalty rate in 3Q21, conditions look set for a new record in Q3 for Iron Valley.

In A\$ terms, the iron ore price averaged \$180.50/t in 2Q21 vs. \$162.80/t in 1Q21. The average price thus far for 3Q21 is \$216.80/t, which bodes well for a very strong 2H21, assuming volumes are up, and the price stays elevated.

Figure 1 shows the 5-year iron ore price in A\$ terms. Current pricing is at record levels and the price really stepped up in mid-December 2020.

Figure 1: Iron ore pricing in A\$



Source: IRESS

BCI HAS LEVERAGE IN IRON ORE FOR 3Q21

We expect all the following to positively impact iron ore related EBITDA in 3Q21:

- A higher iron ore price in A\$ terms (up 26% in 3Q21 to date over 1H21), noting that as the cost base is relatively fixed, a price increase drives the EBITDA line more than the percentage price increase;
- Higher volumes are expected to be shipped; and
- The higher iron ore price results in a higher royalty rate (no costs associated with this).

We forecast that the \$25m EBITDA reduction to fund the cutback is paid in FY21, hence FY22 and onwards forecasts are higher as this cost is removed. We still assume that Iron Valley ceases operating at the end of FY23, though if the iron ore price is still high then, the mine life could be extended.

NAIF STUMPS UP

NAIF has indicated that it is prepared to lend up to \$450m of 15-year debt towards the Mardie project. This is the largest NAIF funding provided for a project in WA. In our opinion, it materially increases the likelihood that BCI can secure FID on the project.

BCI also indicated it has commenced discussions with the Australian Export Finance agency, which also has capacity to provide long term debt. NAIF's better than expected funding component should help attract other banks and equity providers.

FID is contingent on obtaining environmental approvals, expected in 2Q21, not far away now.

BCI's confidence on the potential of Mardie progressing should give confidence to investors

EARLY WORKS COMMENCED

BCI indicated that it is expanding the accommodation village to 80 beds, an indication that BCI is progressing as though the project is going ahead. The 80 beds will facilitate early works and construction of a larger village.

A salt pilot plant is being constructed, with 20t scheduled to be process in the current quarter. This should assist with converting non-binding off-take agreements to binding, with samples to be sent to potential off-take partners.

A SOP pilot plant is expected to be installed in Q2 2021.

APPROVALS THE LAST MAIN HURDLE

Approvals are advanced and there is an expectation they will be granted in 2Q21. Once received, we expect BCI to move to FID. We expect this to be a major catalyst, we have seen other companies rally significantly upon achieving environmental approvals. This is likely to also occur at BCI.

Forecast Earnings Changes

Our Mardie forecasts remain unchanged and don't impact earnings until FY25.

Our Iron Valley forecasts have increased on the back of a higher forecast iron ore price and higher royalty rate. Volumes remain unchanged.

The increased EBITDA (i.e. cashflow) from Iron Valley reduces the amount of equity we forecast that BCI needs to raise, hence reduces dilution. We reduce the amount raised by \$15m.

Our forecast changes impact EBITDA for FY21 to FY23 by \$18m / \$18m and \$13m respectively, see Figure 2. BCI indicated that at the end of 2Q21, they had \$78.5m cash on hand and no debt.

Iron Valley royalty rate and the iron ore price has led to large earnings upgrades

Figure 2: Forecast Changes

\$m	Old			New			Difference		
	FY21F	FY22F	FY23F	FY21F	FY22F	FY23F	FY21F	FY22F	FY23F
Revenue									
Iron Valley	101.8	85.7	72.7	136.2	114.3	94.8	34.4	28.6	22.1
Mardie	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Revenue	101.8	85.7	72.7	136.2	114.3	94.8	34.4	28.6	22.1
Iron Valley	27.3	19.8	13.8	45.5	38.1	26.5	18.2	18.3	12.7
Mardie	(10.0)	0.0	0.0	(10.0)	0.0	0.0	0.0	0.0	0.0
Corporate	(5.6)	(5.8)	(6.1)	(5.6)	(5.8)	(6.1)	0.0	(0.0)	0.0
EBITDA	11.7	13.9	7.7	29.9	32.3	20.4	18.2	18.4	12.7
Depreciation	0.0	(0.3)	(0.6)	(0.0)	(0.3)	(0.6)	(0.0)	0.0	(0.0)
Amortisation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total EBIT	9.1	11.1	4.4	27.3	29.4	17.2	18.2	18.3	12.8
Net Interest	12.1	9.3	0.5	2.8	2.6	(1.1)	(9.3)	(6.7)	(1.6)
Tax	(5.9)	(5.7)	(1.4)	(8.4)	(9.0)	(4.5)	(2.5)	(3.3)	(3.1)
Abnormals	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Reported NPAT	15.3	14.7	3.6	21.7	23.0	11.6	6.4	8.3	8.0
UNPAT Adj. Mardie	25.3	14.7	3.6	31.7	23.0	11.6	6.4	8.3	8.0
Underlying EPS (cps)	2.4	0.9	0.2	3.1	1.4	0.7	0.7	0.5	0.5
Iron Valley Assumptions									
I.V. Tonnes Sold mt	7.5	7.5	7.5	7.5	7.5	7.5	0.0	0.0	0.0
Benchmark Iron Ore US\$/t	108	95	85	134	113	101	26.3	17.9	16.1
I.V. Total Revenue	828	732	655	1,007	847	758	179.2	115.0	103.0
BCI Royalty Rate	5.5%	4.5%	3.5%	7.0%	4.5%	3.5%	1.5%	0.0%	0.0%

Source Pac Partners

Investment view and valuation

We use DCF to value BCI. DCF captures Mardie, Iron Valley and ascribes a value for future iron ore royalties not yet in operation.

DCF

Whilst BCI is still to reach FID and secure all the necessary approvals, securing \$450m of debt from NAIF lowers the funding risk. We lower our risk discount factor to 20% (from 25%) due to achieving a large portion of long-term debt.

Increases in forecast EBITDA from Iron Valley increases our valuation.

Our un-risked DCF valuation moves to \$0.67/share (from \$0.61).

Figure 3: DCF valuation

Present value of cashflows FY20 to FY29	(540)
Present value of terminal year cashflow	1,594
Net Cash at 1H20A	0
NPV of royalties, risk discounted 75%	20
Present value of equity	1,074
Diluted Shares on issue (post raisings)	1,606
Present value per share	\$0.67
20% discount factor	-\$0.13
Discounted DCF Valuation	\$0.53

Source: PAC Partners

Our target price of \$0.53 equates to ~80% upside from the current share price

We set our price target in line with our discounted DCF valuation, which results in a price target of \$0.53/share (from \$0.46). This is ~80% higher than the current share price. We retain our Speculative Buy recommendation and expect once environmental approvals are obtained, BCI should move a lot closer to our price target.

INVESTMENT VIEW

BCI has two large near term catalysts, being:

- Environmental approval; and
- A market re-rating along with many other commodity stocks.

Other smaller catalysts like binding offtake agreements also exist that help de-risk Mardie.

We would also look to review our 20% discount to our DCF valuation post Mardie achieving environmental approvals and remove the discount altogether once FID is achieved.

Relative to Australian SOP start-ups, BCI looks resounding value.

We recommend building a position now. Investors with a long-term horizon, BCI offers excellent value, noting that when fully ramped up and producing ~\$197m EBITDA, peer analysis indicates it could be worth between \$1.75-\$2.45bn.

Financial Model

BCI Minerals						Share Price (\$)	0.295	Mkt Cap: (\$m)	177	Speculative Buy								
PROFIT & LOSS (\$m)	FY19A	FY20A	FY21F	FY22F	FY23F	KEY RATIOS					FY19A	FY20A	FY21F	FY22F	FY23F			
Operating Revenue	54.2	54.2	136.2	114.3	94.8	EBITDA Margin (%)	-4.8%	30.3%	22.0%	28.2%	21.6%	EBIT Margin (%)	-9.6%	24.4%	22.0%	28.0%	20.9%	
EBITDA	(2.6)	16.4	29.9	32.3	20.4	NPAT Margin (%)	23.8%	21.6%	17.8%	22.4%	15.0%	ROE (%) y/e	-3.0%	9.3%	5.2%	5.3%	2.6%	
Depreciation	(0.1)	(0.6)	(0.0)	(0.3)	(0.6)	ROA (%) y/e	-5.4%	14.0%	23.6%	10.4%	3.4%	ROIC (%) Av.	-6.5%	17.2%	34.2%	17.2%	4.6%	
Amortisation	0.0	0.0	0.0	0.0	0.0	NTA per share (\$)	0.13	0.14	0.63	0.67	0.69	Eff Tax Rate (%)	32.9%	28.0%	28.0%	28.0%	28.0%	
EBIT	(5.2)	13.2	29.9	32.0	19.8	EBIT Interest Cover (x)	NM	NM	nm	nm	13.7	Gearing ND/ND+E (%)	(48%)	(66%)	(542%)	(67%)	10%	
Net Interest	0.6	0.3	2.8	2.6	(1.1)	OPCF / EBITDA (%)	237%	27%	35%	37%	102%							
Income tax expense	1.5	(3.8)	(8.4)	(9.0)	(4.5)													
UNPAT pre abnormal	(3.1)	9.7	24.3	25.6	14.2													
Abnormal Items	16.0	2.0	0.0	0.0	0.0													
Reported NPAT	12.9	11.7	24.3	25.6	14.2													
Normalised NPATA	5.1	17.9	31.7	23.0	11.6													

BALANCE SHEET (\$m)	FY19A	FY20A	FY21F	FY22F	FY23F	VALUATION METRICS					FY19A	FY20A	FY21F	FY22F	FY23F			
Cash	33.7	41.5	338.9	163.1	13.1	Dil. Normalised EPS (c)	1.3	4.4	3.1	1.4	0.7	Dil. Reported EPS (c)	3.3	2.9	2.2	1.4	0.7	
PP&E	0.2	2.8	3.0	182.1	436.3	Dil. Normalised PE (x)	22.8	6.6	9.4	20.6	40.9	Dil. Reported PE (x)	9.1	10.2	13.7	20.6	40.9	
Debtors & Inventory	22.3	16.2	51.4	40.9	29.4	Enterprise Value (\$m)	143	135	-160	7	223	EV / EBITDA (x)	-55.0	8.2	-5.4	0.2	10.9	
Intangibles	23.5	18.5	23.5	23.5	23.5	EV / EBITA (x)	-27.4	10.2	-5.4	0.2	11.2	EV / EBIT (x)	-27.4	10.2	-5.4	0.2	11.2	
Other assets	50.7	57.0	37.8	35.2	14.6	Price / NTA (x)	2.2	2.1	0.5	0.4	0.4	DPS (c)	0.0	0.0	0.0	0.0	0.0	
Total Assets	130.4	136.1	454.7	444.9	517.0	Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%	Franking (%)	0%	0%	0%	0%	0%	
Borrowings	0.0	0.0	2.0	(6.5)	59.5	Payout Ratio (%)	0%	0%	0%	0%	0%	Free Cash / Share (cps)	5.2	1.9	0.8	(10.4)	-13.4	
Trade Creditors	18.1	18.3	30.0	22.9	17.1	Price / FCF PS (x)	5.7	15.2	n/m	-2.8	-2.2	Net Debt / EBITDA (x)	13.0	(2.5)	(11.3)	(5.3)	2.3	
Other Liabilities	8.7	13.7	23.6	6.4	6.7													
Total Liabilities	26.8	32.0	55.6	22.8	83.3													
Shareholder Equity	103.6	104.1	399.1	422.1	433.8													

CASHFLOW (\$m)	FY19A	FY20A	FY21F	FY22F	FY23F	GROWTH PROFILE (YoY)					FY19A	FY20A	FY21F	FY22F	FY23F			
Operating EBITDA	(2.6)	16.4	29.9	32.3	20.4	Sales (\$m)	62%	0%	151%	-16%	-17%	EBITDA (\$m)	-82%	-732%	82%	8%	-37%	
Interest & Tax Paid	2.1	0.5	(5.6)	(6.4)	(5.6)	EBIT (\$m)	-70%	-353%	126%	7%	-38%	Adj. NPAT (\$m)	-137%	250%	77%	-27%	-50%	
Working Cap.	(5.7)	(12.5)	(13.7)	(13.8)	6.0	Adj. EPS (c)	-136%	243%	-29%	-54%	-50%	DPS (c)	0%	0%	0%	0%	0%	
Operating CF	(6.2)	4.4	10.6	12.1	20.8													
Maintenance Capex	(0.2)	(3.3)	(0.2)	(0.2)	(0.2)													
Expansion Capex	27.0	6.8	(2.5)	(179.2)	(236.6)													
Free Cashflow (FCF)	20.6	7.8	8.0	(167.3)	(216.0)													
Ord & Pref Dividends	0.0	0.0	0.0	0.0	0.0													
Net Other	0.0	0.0	287.4	0.0	0.0													
Net Cashflow	20.6	7.8	295.4	(167.3)	(216.0)													

DIVISIONAL P&L (\$m)	FY19A	FY20A	FY21F	FY22F	FY23F	DCF VALUATION									
Iron Valley	54.2	54.2	136.2	114.3	94.8	PV of Cashflows FY20-29	(540)	Risk Free Rate	5.0%						
Mardie	0.0	0.0	0.0	0.0	0.0	PV of Term Year Cashflow	1,594	Equity Risk Premium	5.0%						
Other	0.5	0.4	2.9	2.5	0.2	Other	0	Equity Beta (x)	1.10						
Total Revenue	54.7	54.6	139.0	116.9	94.9	Net Cash at 1H20A	0	Cost of Equity	10.5%						
						PV of Equity	1,074	WACC	7.0%						
						PV of Equity per share	\$ 0.67	Terminal Growth	2.5%						

DIRECTORS	%		%
Brian O'Donnell	0.1%	Jenny Bloom	0.0%
Alwyn Vorster	0.9%	Michael Blakiston	0.0%
Garret Dixon	0.0%		
		Total	1.0%

SUBSTANTIAL HOLDERS	%		%
Wroxby Pty Ltd	39.6%	Sandon Capital	6.1%

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RECOMMENDATION CRITERIA

Investment View

PAC Partners Investment View is based on an absolute 1-year total return equal to capital appreciation plus yield.

A Speculative recommendation is when a company has limited experience from which to derive a fundamental investment view.

Buy	Hold	Sell
>20%	20% – 5%	<5%

Risk Rating

PAC Partners has a four tier Risk Rating System consisting of: Very High, High, Medium and Low. The Risk Rating is a subjective rating based on: Management Track Record, Forecasting Risk, Industry Risk and Financial Risk including cash flow analysis.

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