Nickel Mines An Emerging Force

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Nickel Mines has taken a stake in another nickel pig iron development in Indonesia, set to catapult the company to the world stage as the largest pure nickel exposure.

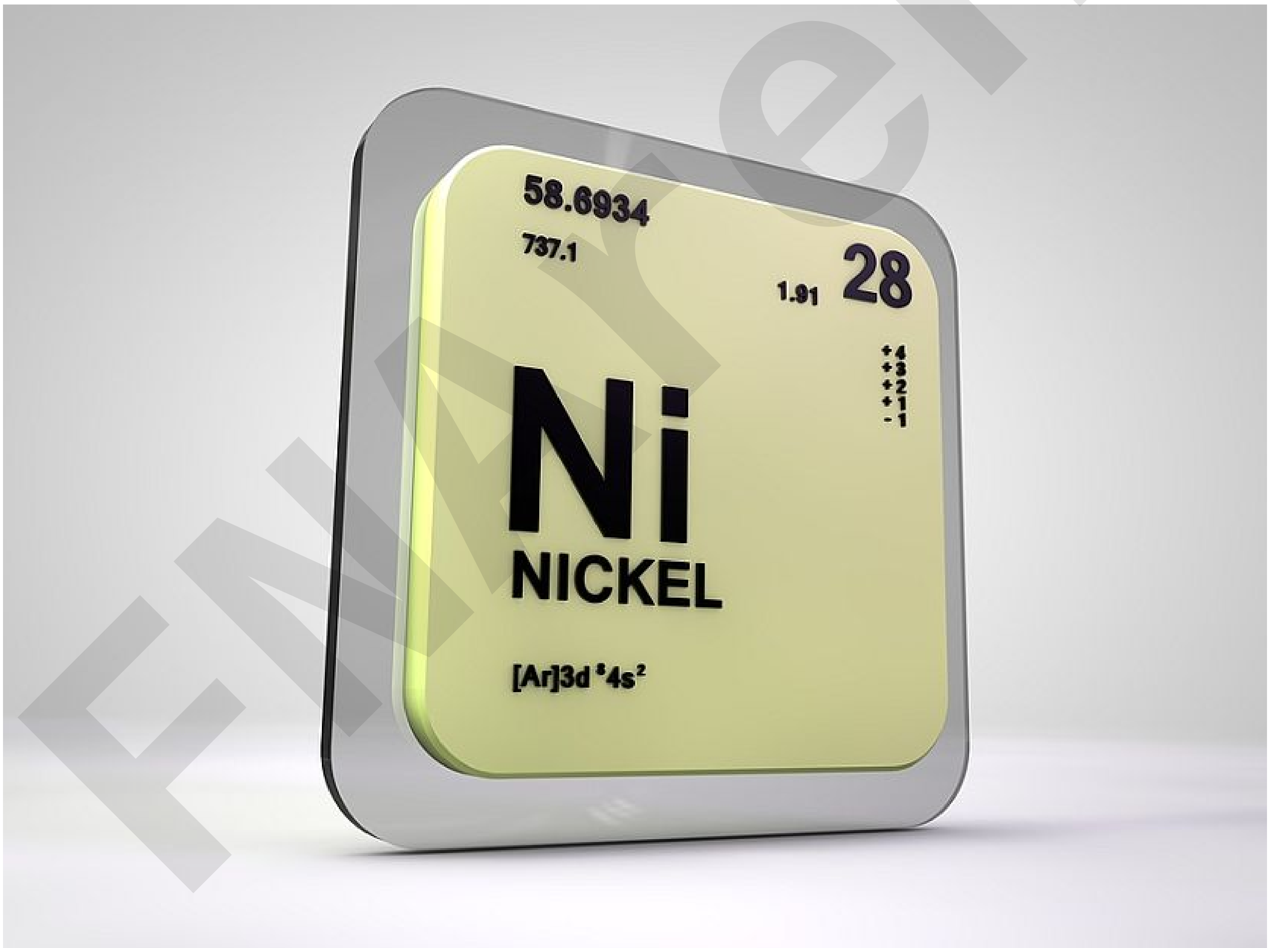
-Highly attractive option with a rapid payback period
-Launching Nickel Mines as the No 6 nickel producer globally
-Hengjaya, Ranger running 20-30% above nameplate

By Eva Brocklehurst

Nickel Mines ((NIC)) is entrenching its position as a major force in nickel globally, with a deal with Tsingshan to develop another facility in Indonesia. The Memorandum of Understanding is with Shanghai Decent Investment (SDI), a subsidiary of Tsingshan, to build, own and operate four new rotary kiln electric furnace (RKEF) lines at the Weda Bay industrial park.

This MOU outlines terms in which Nickel Mines can acquire a 70% interest in PT Angel Nickel Industry for US$490m, a new nickel development with a nameplate capacity of 36,000tpa of contained nickel from nickel pig iron that will also build a 380MW coal-fired power station.

This would imply exposure to an additional 25,200tpa for the company and double its nickel production to 58,000tpa by 2025. The new lines are scheduled to be commissioned in the September quarter of 2022.



Nickel Mines will then be the largest pure nickel exposure and the sixth nickel producer globally, according to Canaccord Genuity's assessment. It already has an 80% interest in two RKEF lines (Hengjaya and Ranger) at Morowali industrial park, 20% owned by Tsingshan.

Bell Potter considers Weda Bay a highly attractive option with the potential for aggressive earnings growth and a rapid payback period, estimated to be under three years. **The company will also obtain lower operating costs from the ownership of the power station** .

Bell Potter, with a Buy rating and $1.52 target, believes this deal is highly value accretive as it allows for efficient growth for Nickel Mines in a market where peers are facing either stable or declining production.

Incorporating the transaction means a 50-70% upgrade to Macquarie's estimates for earnings per share while the dilution, assuming a 50:50 debt:equity funding split, means a -19% and -24% reduction to 2021 and 2022. Nevertheless, buoyant nickel prices drive upside risk to forecasts.

However, Shaw and Partners does not believe Nickel Mines will need to raise equity for the acquisition, assessing existing cash flow forecasts means this can be funded from reserves, future cash flow and US$250m in debt.

The broker has a Buy rating and a $1.33 target and incorporates earnings from Weda Bay in its financial modelling from the second half of 2023. Meanwhile, 2020 forecasts are also upgraded to allow for a stronger nickel price in the second half.

Shanghai Decent will construct and operate the four RKEF lines at Weda Bay along with the power station, and has contractually committed to a maximum cost of US$700m. By way of comparison the existing Morowali ramp-up took 1-2 quarters.

Weda Bay is not directly comparable to Morowali, Macquarie asserts, because it also includes a coal-fired power station while Canaccord expects the company will be granted the same tax concessions.

Canaccord applies a 60% risk consideration in its valuation to account for funding requirements and execution risk, calculating a $1.60 target with a Buy rating.

At Morowali, the Hengjaya mine re-started supply early in 2019 and Ranger in mid 2019 and both now have a steady state production of 22,000tpa of nickel a piece, running at 20-30% above nameplate. Shaw notes Morowali has a cheap source of both nickel ore and power which means costs are highly competitive at around US$7750/t.

Macquarie points out **the Weda Bay transaction does not incorporate any nickel ore supply agreement** and there is some risk, therefore, that it could cost more compared with Hengjaya and Ranger. The broker has an Outperform rating and $1.20 target.

Background

Tsingshan is a major shareholder in Nickel Mines, with 18.6%, and is also the world's largest stainless steel producer. The relationship between Tsingshan and Nickel Mines has meant the latter went from a raw material supplier from the Hengjaya mine to being a partner in building the RKEF capacity at Morowali.

Hence, as Shaw points out, it has become a high-value industrial processor of nickel pig iron. For Tsingshan the benefit was having an Australian-listed entity in which could make a strategic investment.

The Weda Bay complex has already been established with four commissioned RKEF lines and a further eight under construction is part of a strategy by Tsingshan to shift its nickel pig iron production to lower cost operations near the source of raw materials in Indonesia.

See also, Nickel Mines Poised For Price Recovery on July 10, 2020.