

14 Feb 2019

## STRANDLINE RES. LTD (STA)

### Site visit to Fungoni and Tajiri in Tanzania

We recently visited two of the Tanzanian assets of Strandline Res. Ltd (STA). Tanzania is very prospective for mineral sands, located on the East Coast of Africa.

In our interaction with locals during our trip (taxi drivers etc) there was widely held view that the Tanzanian Government is now pro-mining. Conversations with local businessmen and officials introduced to us by STA were certainly confident that the Fungoni project will be developed and that the Government was now actively trying to accelerate mining investment.

### Fungoni – starter zircon rich project with chloride ilmenite

Fungoni (79-84%) is a low capex zircon project in Tanzania (reserve 12.3Mt @ 3.9%THM). The project was recently granted a mining licence, and the DFS is completed with offtakes in place for most of the products. Capex is estimated at US\$32m (~A\$42m). The DFS estimates EBITDA ~A\$25m pa (100%). The mine life is relatively short though at ~6 years. We assume start-up capital ~A\$44m (8yr mine life), EBITDA of ~A\$21m pa (\$17m attrib.) or on spot prices A\$27m pa (A\$21m attrib.). Production is possible in CY20, subject to financing.

We were impressed with the location of Fungoni, with straightforward public road access to port. Dar es Salaam, as a very large city, we had worried that road access between site and the port would be difficult. However, the city extends to the North of the port, whereas Fungoni is South of the port. The city to the South very quickly becomes countryside and the roads, while unsealed, are uncongested.

Equally, the Fungoni project appears like it should have limited social impact and agreements with landholders should be straightforward. Obviously, a key benefit of mineral sands mining is the ability to completely rehabilitate land.

### Tajiri – large exploration potential

Tajiri (79-84%) has a resource of 147Mt @ 3.1% THM and an exploration target for an additional 73-133Mt @ 2.8-4.4% THM. Access is more difficult than Fungoni, and Port infrastructure is yet to be determined (there is the option of the Tanga port). The project is still in exploration phase / pre-scoping and hence these issues can be resolved once the project is properly defined and scoped. It appeared to us that there would be limited social impact and much of the ground are [sisal](#) plantations.

### Retain Speculative Buy

We retain our Speculative Buy. Using our base mineral sands prices, our valuation (NPV<sub>12</sub>, our standard discount rate for this stage) is 20cps, diluted for ~1.1b new shares to develop Fungoni and the larger Coburn project.

If, instead, we assume Coburn (Aust.) and Tajiri (Tanzania) are undeveloped and attribute minimal value, and then only dilute for the development of Fungoni (230m new shares), our valuation is 11cps. Hence, at current levels it implies STA is valuing only Fungoni, and not the larger potential for STA. We assume A\$22m of new equity is required for Fungoni, but the Company is hopeful for a higher debt proportion.

Share Price	\$0.097
Preliminary valuation	\$0.20
Price Target (12 month)	\$0.22

#### Brief Business Description:

Mineral sands developer in Tanzania and Australia.

#### Hartleys Brief Investment Conclusion

STA has potential to build substantial mineral sands business in Tanzania. The Fungoni development is an attractive zircon rich project in Tanzania. Coburn is a large, low grade, WA asset.

#### Chairman & MD

Didier Murcia (Non Exec-Chairman)

Luke Graham (MD)

#### Top Shareholders

Tembo	35.9%
C&H Investments	9.7%
Gasmere / Hatch	7.3%

#### Company Address

35 Richardson St  
 West Perth, WA 6005

Issued Capital 320.7m

- fully diluted 373.3m

Market Cap A\$31.1m

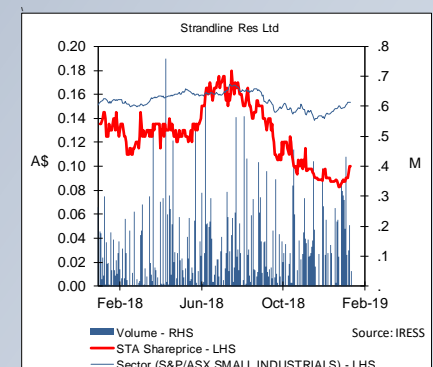
- fully diluted A\$36.2m

Cash (31 Dec 18a) A\$4.2m

Debt (31 Dec 18a) A\$0.0m

EV A\$26.9m

	FY19e	FY20e	FY21e
EBITDA	-1.9	2.0	29.4
Op Cash Flw	-3.2	1.5	27.2
Norm NPAT	-3.6	-3.1	10.9
CF/Share (cps)	-0.8	0.2	1.9
EPS (cps)	-0.9	-0.3	0.8
P/E	-10.4	-30.0	12.8



Trent Barnett

Head of Research

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Hartleys has assisted in the completion of a capital raising in the past 12 months for Strandline Resources Limited ("Strandline") for which it has earned gross fees. Hartleys has a beneficial interest in fully paid ordinary shares Strandline Resources Limited. See back page for disclosure

Strandline Res Ltd						Share Price		14 February 2019					
STA						\$0.097		Speculative Buy					
<b>Key Market Information</b>						<b>Company Information</b>							
<b>Share Price</b>						<b>Directors</b>							
Market Capitalisation - ordinary						Didier Murcia (Non Exec-Chairman)							
Net Debt (cash)						Luke Graham (MD)							
Market Capitalisation - fully diluted						Peter Watson (Exec Director)							
EV						Earnest (Tom) Eadie (Non- Exec Director)							
EV inc. assumed new capital						John Hodder (Non- Exec Director, Tembo nominee)							
Issued Capital						www.strandline.com.au							
Options						<b>Top Shareholders</b>							
Issued Capital (fully diluted inc. all options)						m shares %							
Issued Capital (fully diluted inc. all options and new capital)						Tembo 115.2 35.9%							
Valuation						C&H Investments 31.3 9.7%							
12month price target						Gasmere / Hatch 23.5 7.3%							
P&L						<b>Reserves &amp; Resources</b>							
Net Revenue						Mt Grade Ilmenite Zircon Rutile/Hiti							
Total Costs						Total Resource 1775 1.4% 49.8% 21.5% 11.8%							
EBITDA						Fungoni Tanzania 22 2.8% 41% 17% 6%							
- margin						Tanga Sth Tanzania 147 3.1% 71% 6% 10%							
Depreciation/Amort						Coburn WA 1606 1.20%							
EBIT						<b>Total Reserve</b>							
Net Interest						Fungoni Tanzania 12 3.9%							
Pre-Tax Profit						Tanga Sth Tanzania 0							
Tax Expense						Coburn WA 308 1.2% 48% 23% 12%							
Normalised NPAT						<b>Coburn Production Summary</b>							
Abnormal Items						Unit Jun 19 Jun 20 Jun 21 Jun 22 Jun 23							
Reported Profit						Mining Inventory Mt 460.1 458.8 438.8 415.4							
Minority						% 1.3% 1.3% 1.3% 1.3%							
Profit Attrib						Mill Throughput Mt 1.3 20.1 23.4							
Balance Sheet						HM grade % 1.3% 1.3% 1.3%							
Cash						Zr production kt 2.6 41.7 48.6							
Other Current Assets						Rutile / Hi-Ti production kt 1.2 19.3 22.6							
Total Current Assets						Chlor. Ilmenite production kt 5.7 90.9 106.1							
Property, Plant & Equip.						Ilmenite % rev. 19.5% 19.4% 19.5%							
Exploration						Zircon % rev. 60.2% 60.0% 59.2%							
Investments/other						Rutile / Hi-Ti production % rev. 20.3% 20.6% 21.2%							
Tot Non-Curr. Assets						Monazite % rev. 0.0% 0.0% 0.0%							
Total Assets						<b>Fungoni Production Summary</b>							
Short Term Borrowings						Unit Jun 19 Jun 20 Jun 21 Jun 22 Jun 23							
Other						Mining Inventory Mt 15.4 15.0 13.0 11.0 9.0							
Total Curr. Liabilities						% 3.7% 3.7% 3.7% 3.4% 3.0%							
Long Term Borrowings						Mill Throughput Mt 0.4 2.0 2.0 2.0							
Other						HM grade % 3.9% 5.3% 5.5% 4.2%							
Total Non-Curr. Liabil.						Zr production kt 2.5 14.4 18.3 17.7							
Total Liabilities						Rutile / Hi-Ti production kt 0.6 3.2 4.1 4.0							
Net Assets						Chlor. Ilmenite production kt 5.6 32.6 41.4 40.0							
Net Debt						Ilmenite % rev. 21.9% 21.3% 20.7% 20.8%							
Cashflow						Zircon % rev. 61.4% 61.5% 61.6% 60.8%							
Operating Cashflow						Rutile / Hi-Ti production % rev. 9.6% 10.0% 10.5% 10.9%							
Income Tax Paid						Monazite % rev. 7.1% 7.2% 7.2% 7.5%							
Interest & Other						<b>Price Assumptions</b>							
Operating Activities						Unit Jun 19 Jun 20 Jun 21 Jun 22 Jun 23							
Property, Plant & Equip.						AUDUSD USD/AUD 0.72 0.75 0.77 0.79 0.78							
Investment Activities						Ilmenite US\$/t fob Tanz 193 203 204 204 197							
Borrowings						Zircon US\$/t fob Tanz 1432 1485 1479 1486 1395							
Equity or "bc capital"						Rutile US\$/t fob Tanz 1001 1061 1121 1178 1160							
Dividends Paid						Leucoxene US\$/t fob Tanz 744 790 835 877 864							
Financing Activities						Monazite US\$/t fob Tanz 1975 1975 1975 1975 1975							
Net Cashflow						<b>Sensitivity Analysis</b>							
Shares						Valuation 0.20 FY22 NPAT 56.9							
Ordinary Shares - End						Spot Prices 0.32 (59.2%) 78.8 (38.5%)							
Ordinary Shares - W'ted						Spot USD/AUD 0.71, Sulphate Ilmenite cfr \$175/t, Chloride Ilmenite cfr \$265/t, Zircon \$1550/t, Rutile \$1150/t.							
Diluted Shares - W'ted						AUDUSD +/-10% 0.13 / 0.28 (-34.3% / 41.0%) 41.6 / 75.6 (-26.8% / 32.8%)							
Ratio Analysis						Ilmenite +/-10% 0.21 / 0.18 (7.9% / -7.6%) 56.9 / 56.9 (0.0% / 0.0%)							
Cashflow Per Share						chloride ilmenite +/-10% 0.21 / 0.19 (5.6% / -5.3%) 60.8 / 53.0 (6.9% / -6.9%)							
Cashflow Multiple						Zircon +/-10% 0.24 / 0.16 (18.5% / -18.7%) 68.0 / 46.5 (19.4% / -18.3%)							
EV (+ cap.) / EBIT						Rutile +/-10% 0.22 / 0.18 (10.6% / -10.8%) 59.4 / 54.4 (4.4% / -4.4%)							
EV (+ cap.) / EBITDA						Leucoxene +/-10% 0.20 / 0.20 (1.2% / -1.0%) 57.7 / 56.1 (1.4% / -1.4%)							
Earnings Per Share						Operating Costs +/-10% 0.15 / 0.25 (-23.7% / 23.9%) 48.6 / 65.2 (-14.6% / 14.6%)							
Price to Earnings Ratio						Production +/-10% 0.28 / 0.12 (41.9% / -42.2%) 72.5 / 40.9 (27.3% / -28.2%)							
Dividends Per Share						<b>Unpaid Capital</b>							
Dividend Yield						Year Expires No. (m) \$m % ord							
Net Debt / Net Debt + Equity %						30-Jun-19 0.0 0.0 0%							
Interest Cover						30-Jun-20 39.7 6.4 12%							
Return on Equity						30-Jun-21 12.9 0.0 4%							
						30-Jun-22 0.0 0.0 0%							
						30-Jun-23 0.0 0.0 0%							
						30-Jun-24 0.0 0.0 0%							
						TOTAL 52.6 6.4 16%							
						<b>Valuation</b>							
						\$m /shr							
						Fungoni 66 0.04							
						100% Coburn (pre-tax NAV at disc. rate of 12%) 191 0.12							
						Tanga Sth 114 0.07							
						Other Assets/Exploration 5 0.00							
						Forwards 0 0.00							
						Corporate Overheads -24 -0.02							
						Net Cash (Debt) 4 0.00							
						Tax (NPV future liability) -54 -0.03							
						Options & Other Equity 6 0.00							
						Total 307 0.20							
Analyst: Trent Barnett													
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*bc capital* could be equity or debt. Our valuation is risk-adjusted for how this may be obtained.													
Sources: IRESS, Company Information, Hartleys Research													

Fig. 2: *Fungoni Site Visit Video – click to view*



Source: Hartleys Research

Fig. 3: *Tajiri Site Visit Video – click to view*



Source: Hartleys Research

*Fig. 4: Fungoni – Road access better than we had expected*



Source: Hartleys Research

*Fig. 5: Fungoni – non descript landscape*



Source: Hartleys Research

## VALUATION

Our base valuation assumes the development of both Fungoni and Coburn, which therefore assumes significant dilution. We assume Fungoni financing in FY19 with first production in March 2020. We assume Coburn is financed in FY20, with first production in June 2021.

We assume mineral sands prices similar to consensus, which is now lower than spot prices. Our base valuation is diluted by Coburn, which is only marginal on our base case assumptions.

However, using spot prices, Coburn becomes a big value driver for STA. Additionally, we model Coburn using the study parameters. A re-optimised DFS potentially could improve the economics even using lower than spot mineral sands prices.

Our model assumes 95% of free cash flow until capital and debt is repaid, and then 79% project ownership. We assume no explicit residual value (but we attribute exploration value to other Tanzania assets).

**Fig. 6: Key assumptions and risks for valuation**

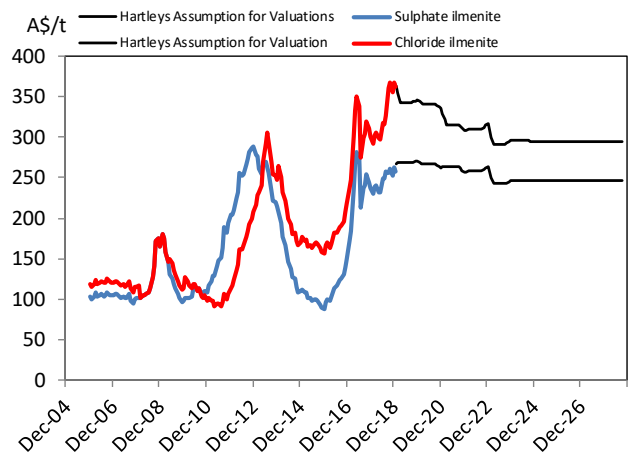
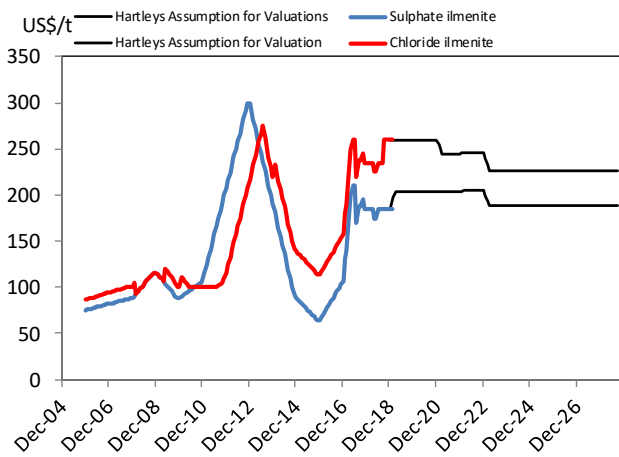
Assumption	Risk of not realising assumption	Risk to valuation if assumption is incorrect	Comment
Fungoni & Coburn are developed	High	High	We assume both assets are developed
Equity dilution	Low	High	We assume ~800m new shares to develop both Fungoni and Coburn. This implies both projects also obtain debt financing
79% project ownership	Low	upside	We assume STA funds 95% of the capital (free carries Govt 16% interest but not the local partners interest), but the capital is repaid (including equity) before the Govt earns dividends.
Commodity prices	Moderate	High	We assume improving AUD rutile prices and ilmenite prices but weaker AUD zircon prices
AUD appreciated modestly	High	Upside / Downside	Using current FX Coburn is substantially more viable. We assume modestly appreciated AUD. Further depreciation though would improve our STA valuation
Value for Tajiri	Moderate	High	We have a speculative unfunded model for Tajiri and use NPV14 given the speculative assumptions.
RIO options not exercised	Moderate	Upside	We don't assume the RIO options are exercised. This is purely to simplify our valuation. Exercise would increase STA cash balance.
Exploration success	Moderate	High	We attribute some value to exploration potential beyond the assumed mine life extension.

*Conclusion*

*We believe our STA assumptions are realistic but given the risks and assumptions we rate it as a Speculative Buy.*

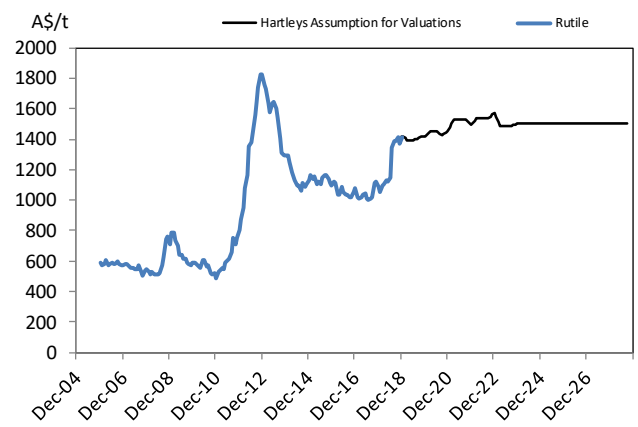
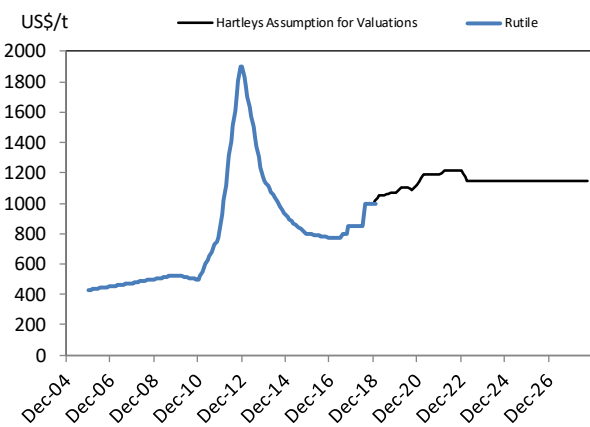
Source: Hartleys Research

**Fig. 7: Ilmenite Price Assumptions**



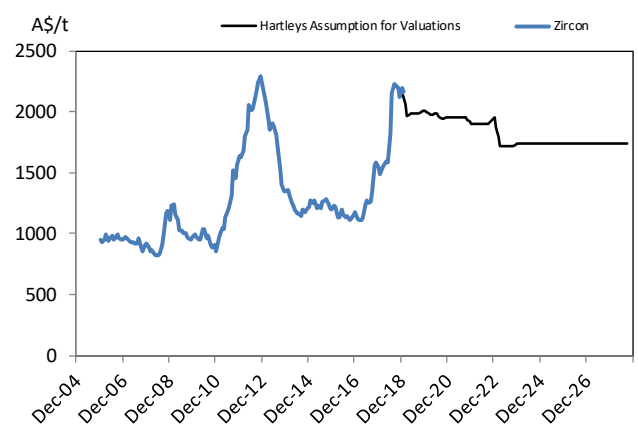
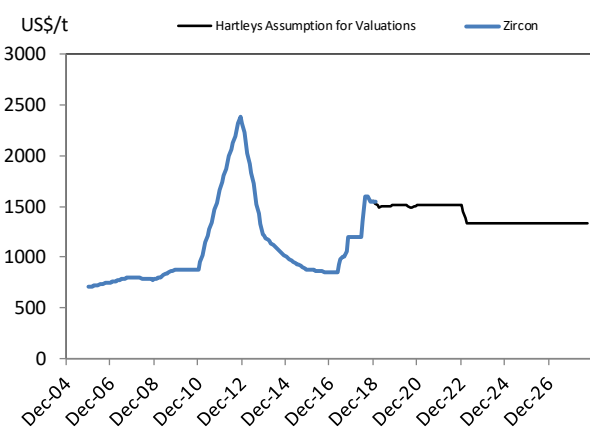
Source: BSE, ILU, Hartleys estimates

**Fig. 8: Rutile Price Assumptions**



Source: BSE, Hartleys estimates

**Fig. 9: Zircon Price Assumptions**



Source: BSE, Hartleys estimates

## PRICE TARGET

Our price target is 22cps (previously 24cps).

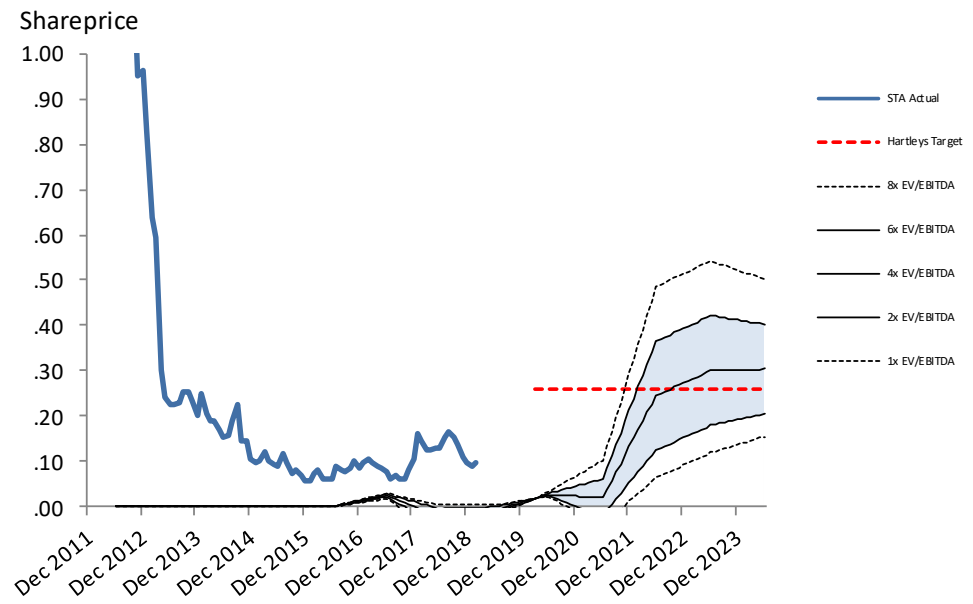
Price Target Methodology	Weighting	Spot	12 mth out
NPV <sub>12</sub> (Fungoni + Coburn) consensus prices	30%	\$0.20	\$0.23
NPV <sub>12</sub> at spot commodity and fx prices	20%	\$0.32	\$0.36
NPV <sub>8</sub> consensus prices	5%	\$0.37	\$0.41
NPV <sub>8</sub> at spot commodity and fx prices	1%	\$0.55	\$0.60
NPV <sub>12</sub> (Fungoni development only, exploration value other assets) base commod.	35%	\$0.11	\$0.13
NPV <sub>12</sub> , minimal dilution, divest Coburn for 50% of NPV (implied STA mcap \$170m)	3%	\$0.28	\$0.33
Net cash backing	6%	\$0.01	\$0.01
<b>Risk weighted composite</b>		<b>\$0.20</b>	
<b>12 Months Price Target</b>		<b>\$0.22</b>	
Shareprice - Last		\$0.097	
<b>12 mth total return</b>		<b>129%</b>	

## RISKS

The key risks for STA (like most mine companies in development) is obtaining the necessary funding to complete the project. Other risks are earnings disappointments given the industry is volatile and earnings can disappoint due to cost overruns, project delays, cost inflation, environmental regulations, plant and mine design mistakes or lower production. Although some earnings disappointments can be short term and are only a timing issue, other disappointments can be materially value destructive and can sometimes overhang stocks for a long period of time (for example metallurgy problems). Such disappointments can be very difficult to predict and share price reactions can be severe and immediate upon disclosure by the company. High financial leverage (if it exists at that time) would add to the problem. Sovereign risk is also reasonably high in Africa.

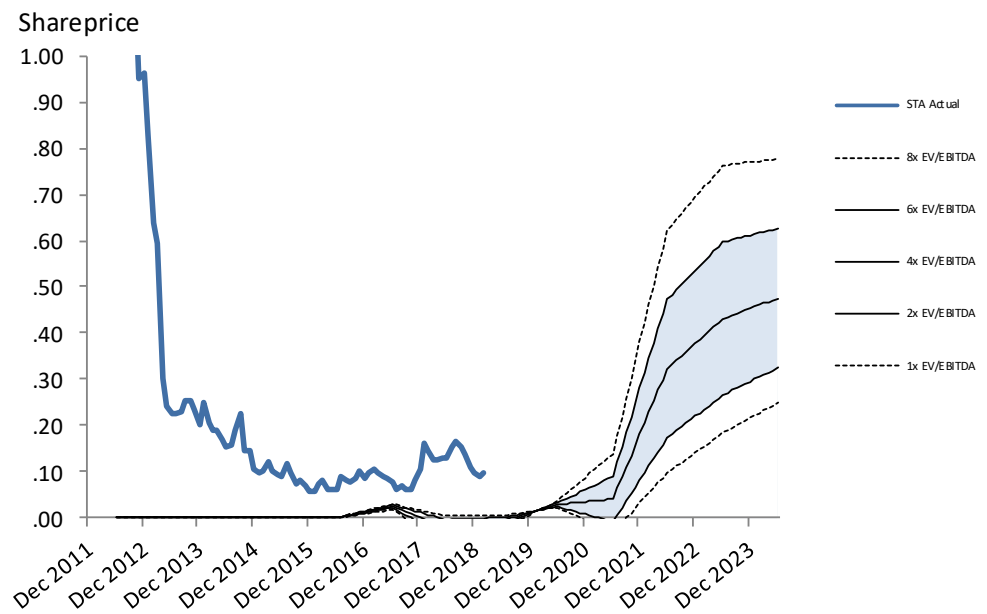
## EV/EBITDA BANDS

**Fig. 10: EV/EBITDA Base case**



Source: Hartleys Estimates

**Fig. 11: EV/EBITDA spot case**



Source: Hartleys Estimates



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*Note: personal email addresses of company employees are structured in the following manner: firstname.lastname@hartleys.com.au*

## Hartleys Recommendation Categories

Buy	Share price appreciation anticipated.
Accumulate	Share price appreciation anticipated but the risk/reward is not as attractive as a "Buy". Alternatively, for the share price to rise it may be contingent on the outcome of an uncertain or distant event. Analyst will often indicate a price level at which it may become a "Buy".
Neutral	Take no action. Upside & downside risk/reward is evenly balanced.
Reduce / Take profits	It is anticipated to be unlikely that there will be gains over the investment time horizon but there is a possibility of some price weakness over that period.
Sell	Significant price depreciation anticipated.
No Rating	No recommendation.
Speculative Buy	Share price could be volatile. While it is anticipated that, on a risk/reward basis, an investment is attractive, there is at least one identifiable risk that has a meaningful possibility of occurring, which, if it did occur, could lead to significant share price reduction. Consequently, the investment is considered high risk.

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