FOSTER STOCKBROKING

EQUITY RESEARCH

Materials

26 November 2021

Strandline Resources Ltd (STA.ASX)

Contracts de-risk Coburn as prices strengthen

Event:

- **Coburn progress; Commodity upgrades; Earnings and PT changes.**

Investment Highlights:

- **STA states that 65% of all operating costs are now locked in at, or below, DFS assumptions** following recent contract awards which now include port, logistics, mining services, power, gas, and fuel. We expect this provides a contingency against remaining costs – mostly labour and spares.
- **Most recent contract award was logistics to Qube Bulk earlier this week.** Qube will provide a turn-key solution, operating haulage fleet, storage facilities, and coordinating port loading, with zircon concentrate and ilmenite stored berth-side at Port of Geraldton, and rutile and premium zircon at Narngulu, only ca. 10km from the Port. Terms are in-line with DFS cost assumptions.
- **Mining services contract awarded in October to Mine Site Construction Services (MSCS).** STA stated rates were in-line with DFS assumptions. Other milestones achieved include construction of the 270-person permanent accommodation camp and deliveries of HDPE piping. Macmahon is progressing civil bulk earthworks, while power station, dozer mining units, and process plant EPC all advancing.
- **Well-funded to completion.** We estimate $54M of capex has been spent to end September 2021, with balance being $210M (we assume $264M total capex). STA funds available were $302M end September ($71M cash plus $231M undrawn debt). We estimate funds are sufficient to cover capex balance, plus working capital, finance costs, exploration, corporate and cost overruns.
- **STA reiterated scheduled first HMC product commissioning in 4QCY22**. The project was 28% complete at end September.
- **We upgrade our mineral sand price forecasts**, with revisions of +7% to +14% over FY22e-FY24e, as well as upgrading LT by 9% for zircon, 5% for rutile, and 13% for ilmenite. Producers have reported price increases across all products, most markedly for zircon, with spot premium zircon price US$2,235/t – still above our forecasts. Increasing tile production and pigment demand coupled with tight supply are supporting prices strength.

Earnings and Valuation:

- **Earnings upgrade on higher prices.** We upgrade FY23e NPAT to $1M from -$9M loss, and FY24e – first full year of Coburn production - by 40% to $63M from $45M on higher minerals sands prices.
- **Risked share valuation (0.8x NPV$_{10}$) increases to $0.62 from $0.52,** on the back of higher prices. On FY24e earnings, STA is trading at 4.5x P/E and 3.4x EBITDA vs ASX Resources of 13.6x and 5.8x for FY23e, supporting our view on stock being undervalued. Meanwhile, running spot zircon yields $0.92 share valuation.

Recommendation:

- **We maintain our Buy and raise our 12-month PT to $0.62 (prior $0.52), in-line with our risked share valuation.**
- **Catalysts for the share price include:** 1) Further Coburn progress; 2) Resource and Reserves upgrades; 3) Coburn commissioning; 4) Progress on Tanzanian assets; and 5) higher mineral sands prices.

Disclosures

The analyst owns 265,500 STA shares.
Foster Stockbroking and associated entities (excluding Cranport Pty Ltd) own 2,265,500 STA shares.
Cranport Pty Ltd owns 9,790,444 STA shares.
Refer details end of report.
Foster Stockbroking acted as Co-Manager and Sub-Underwriter to the $122M placement and entitlement offer of 593M STA shares at $0.205 in March 2021, for which it received fees.

Recommendation	**Buy**
Previous	Buy
Risk	High
Price Target	**$ 0.62**
Previous	$0.52
Share price (A$)	**$ 0.245**
ASX code	STA
52 week low-high	$0.165-$0.298
Valuation - risked (A$/share)	**$ 0.62**
Methodology	risked NPV
Capital structure	
Shares on Issue (M)	1,120
Market cap (A$M)	274
Net cash (debt) (A$M)	71
Performance rights (M)	8
Options (M)	11
Diliuted EV (A$M)	208
Ave daily volume ('000)	2,689

Earnings Y/e Jun A$M	FY21a	FY22e	FY23e	FY24e
Sales	0	0	50	203
EBITDA adj	-12	-7	19	101
NPAT reported	-13	-15	1	63
NPAT adj	**-13**	**-15**	**1**	**63**
EPS adj. $*	**-0.02**	**-0.01**	**0.00**	**0.05**
PE x	**nm**	**nm**	**nm**	**4.5x**
EV/EBITDA x	nm	nm	18.2x	3.5x

** Adj =underlying*

Substantial shareholders	
Ndovu Capital VII BV (Tembo)	21%
Regal Funds Management Pty Ltd	5%

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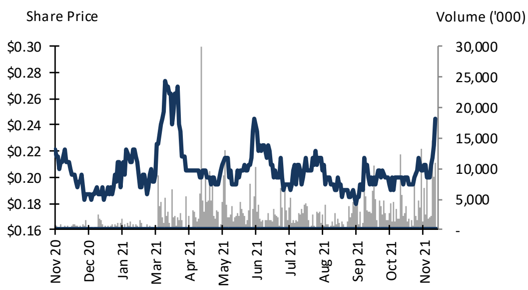
Mark Hancock	Non-Executive Director
Alexandra Atkins	Non-Executive Director
Tom Eadie	Non-Executive Director

Share price graph



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Strandline Resources (STA)

Full Year Ended 30 June

Profit and Loss A$M	2021a	2022e	2023e	2024e
Revenue	0	0	50	203
Operating Costs adj.	12	7	31	101
EBITDA adj.	**-12**	**-7**	**19**	**101**
D&A	0	0	3	12
EBIT adj.	**-12**	**-7**	**16**	**89**
Net Interest exp / (income)	1	8	14	16
PBT adj.	**-13**	**-15**	**2**	**73**
Tax exp / (benefit) adj.	0	0	1	10
NPAT adj.	**-13**	**-15**	**1**	**63**
Non-recurring items	0	0	0	0
NPAT reported	**-13**	**-15**	**1**	**63**
EPS diluted ($) adj.	**-0.02**	**-0.01**	**0.00**	**0.05**

Cashflow A$M	2021a	2022e	2023e	2024e
EBITDA adj.	0	0	50	203
Change in WC	10	-14	-2	-7
Tax paid	0	0	-1	-10
Other	-7	0	0	0
Net interest	-2	-8	-14	-16
Share based payments	1	1	1	1
Operating Cashflow	**-10**	**-28**	**3**	**69**
Purchase of PP&E	-2	-2	0	-3
Acquisitions	0	0	0	0
Capitalised expenses	-12	-164	-89	0
Investments	0	0	0	0
Investing Cashflow	**-14**	**-165**	**-89**	**-3**
Equity issue	140	0	0	0
Debt proceeds	3	210	0	0
Debt repayments	0	0	0	-11
Other	-12	6	0	0
Financing Cashflow	**130**	**216**	**0**	**-11**
Net Cashflow	**106**	**22**	**-86**	**55**

Balance Sheet A$M	2021a	2022e	2023e	2024e
Cash	116	139	53	108
Receivables	1	0	4	17
PPE	0	0	290	280
Capitalised exploration	37	201	0	0
Intangibles	0	0	0	0
Other	2	0	0	0
Total Assets	**156**	**339**	**347**	**405**
Accounts payable	16	1	3	8
Provisions	2	1	3	8
Debt	3	213	213	202
Other	0	5	7	3
Total Liabilities	**22**	**219**	**225**	**221**
Reserves and capital	221	221	221	221
Retained earnings	-86	-101	-100	-37
Total Equity	**135**	**120**	**121**	**184**

Capital structure	M
Ordinary shares	1,120
Performance rights	8
Options	11
Fully diluted	**1,139**

Financial Metrics	2021a	2022e	2023e	2024e
Sales growth %	nm	nm	nm	305%
EPS growth %	nm	nm	nm	nm
EBITDA margin	nm	nm	38%	50%
EBIT margin	nm	nm	32%	44%
Gearing (ND/ND+E)	nm	38%	57%	34%
Interest Cover (EBIT/net int)	nm	-1x	1x	6x
Average ROE %	-10%	-12%	1%	41%
Average ROA %	-8%	-3%	5%	24%
Wtd ave shares (M)	645	1,120	1,120	1,120
Wtd ave share diluted (M)	669	1,139	1,139	1,139

Valuation multiples	2021a	2022e	2023e	2024e
P/E x	**nm**	**nm**	**nm**	**4.5**
EV/EBITDA x	**nm**	**nm**	**18.2**	**3.5**

Company Valuation

DCF, WACC 10% nominal

Segment	Unrisked A$M	Unrisked A$/sh	Risked A$M	Risked A$/sh
Coburn Reserves	496	$0.44	471	$0.41
Coburn Expansion	112	$0.10	84	$0.07
Fungoni (84%)	32	$0.03	21	$0.02
Tajiri (84%)	205	$0.18	103	$0.09
Corporate	-51	-$0.04	-48	-$0.04
Other Tanzania exploration	15	$0.01	5	$0.00
Net cash (debt)	71	$0.06	71	$0.06
Cash from in money options	2	$0.00	2	$0.00
Total	**883**	**$0.78**	**709**	**$0.62**

Shares now M	1,120
Performance rights M	8
Options-in-money at valuation M	11
Fully diluted shares M	**1,139**

Commodity Assumptions	2021a	2022e	2023e	2024e
Prices (US$/t)				
Zircon	1,458	1,602	1,708	1,711
Ilmenite - chloride grade	229	246	259	268
Rutile/HiTi	1,217	1,273	1,310	1,304
Monazite	1,427	1,456	1,485	1,514
A$/U$	0.72	0.75	0.75	0.74
Shipments (kt)				
Zircon	0	0	9	34
Zircon concentrate	0	0	14	54
HiTi90	0	0	6	24
Ilmenite	0	0	28	110
Total	**0**	**0**	**56**	**222**
Revenue to C1 cost ratio	0.0	0.0	2.5	2.5

Segment Contribution	2021a	2022e	2023e	2024e
Coburn	0	0	50	203
Tanzania	0	0	0	0
Sales	**0**	**0**	**50**	**203**
Coburn	0	0	24	98
Tanzania	0	0	0	0
Corporate & expl'n	-8	-12	-8	-9
Group EBIT	**-8**	**-12**	**16**	**89**

Source: Company; Foster Stockbroking estimates

COBURN POSITIVE PROGRESS

Contract costs in-line or below DFS

- STA reported Coburn continuing to align with budget, following recent awards of a number of contracts. The company stated that 65% of all operating costs locked in at, or below, DFS forecast, with all major contracts now awarded. These include port, logistics, mining services, gas, fuel, and port. These also provide some natural contingency against the balance of operating costs, which we believe mostly relates to labour and spares.

Logistics award

- The most recent contract finalised was logistics earlier this week, it being awarded to Qube Bulk, Australia's largest dedicated bulk logistics services provider. Qube will undertake product transport and storage under a turn-key solution, operating the haulage fleet, storage facilities, and coordinating port loading. Qube will store Coburn's largest volume products – zircon concentrate and ilmenite - berth-side at Port of Geraldton, and the rutile and premium zircon at Narngulu, located only ca. 10km from the Port. Contract terms are in accordance with cost assumptions of the DFS.

Mining contract

- In October STA awarded the Coburn mining services contract to Mine Site Construction Services (MSCS), who will operate the mine fleet associated with both mining and backfilling. STA stated rates were in-line with DFS assumptions.
- Other major contracts and milestones achieved include:
    - Construction of the 270-person permanent accommodation camp – with first 100 rooms commissioned.
    - First deliveries of HDPE piping.
    - Deliveries of overhead power lines.
    - Supply of LNG.
    - Macmahon progressing civil bulk earthworks, including site earthwork pads for site roads, WCP and MSP areas.
    - Hybrid power station, dozer mining units, and processing plant EPC works all advancing. All major mechanical equipment ordered and design reviews and fabrication underway.
    - Multiple bore drilling contractors mobilised, installation of water bores progressing.

Well-funded to completion

- We estimate $54M of capex has been spent to end September 2021, with balance being $210M (we assume $264M total capex). STA funds available were $302M end September ($71M cash plus $231M undrawn debt facilities). We estimate funds are sufficient to cover balance of capex, plus working capital, finance costs, exploration, corporate and cost overruns (Figure 1). We expect debt will be drawn once cash equity has been mostly utilised, pro-rata from NAIF and Nordic bond.

Figure 1: STA Funds Balance and Remaining Expenditure as at 30 September 2021

Available funds	A$ M	Remaining expenditure	A$M
Cash	71	Capex	210
NAIF debt undrawn	150	Working capital	15
Nordic bond undrawn	81	Corporate	8
		Finance costs	25
		Exploration	3
		Other incl. cost overruns/further contigency	41
Total	**302**	**Total**	**302**

Source: Company; Foster stockbroking estimates.

4QCY22 commissioning reiterated

- STA reiterated the Coburn project is tracking on-time for scheduled first HMC product commissioning in 4QCY22. The project was 28% complete at end September.

Infill results derisks mine plan

- In September STA reported infill drill results targeting the first two years of Coburn production, akin to grade control. Results confirmed the integrity of the resource model mineralisation, while some of the shallow mineralised intercepts extended outside the mine or Reserves envelope. This provides scope for a potential Resource upgrade, including re-classifying Indicated to Measured, and to upgrade Reserves by moving Probable to Proved, enhancing the mine plan in the first two years.

Tanzania framework progresses

- The company continues progressing its Tanzanian minerals sands projects by engaging with the Government to finalise a Framework Agreement. This would detail terms for joint ventures for Fungoni and Tajiri, with the company also seeking a Special Mining Licence for the latter. Conclusion of the Framework Agreement would allow STA to accelerate commercialisation of its Tanzanian assets.

MINERAL SANDS PRICE UPGRADES

- We have upgraded our mineral sand price forecasts, with revisions of +7% to +14% up over FY223-FY24e, as well as upgrading our LT assumptions by 9% for zircon, 5% for rutile, and 13% for ilmenite (Figure 2).

Figure 2: Mineral sands commodity price forecasts (US$/t)

Commodity		FY21a	FY22e	FY23e	FY24e	LT nom.
Zircon premium	**New**	**1,458**	**1,602**	**1,708**	**1,711**	**1,644**
	Old	*1,475*	*1,495*	*1,497*	*1,495*	*1,505*
	Chng	*-1%*	*7%*	*14%*	*14%*	*9%*
Zircon concentrate	**New**	**493**	**536**	**571**	**572**	**550**
	Old	*493*	*500*	*501*	*500*	*503*
	Chng	*0%*	*7%*	*14%*	*14%*	*9%*
Rutile	**New**	**1,217**	**1,273**	**1,310**	**1,304**	**1,307**
	Old	*1,169*	*1,186*	*1,221*	*1,232*	*1,247*
	Chng	*4%*	*7%*	*7%*	*6%*	*5%*
Ilmenite - chloride	**New**	**229**	**246**	**259**	**268**	**273**
	Old	*221*	*223*	*229*	*235*	*242*
	Chng	*4%*	*10%*	*13%*	*14%*	*13%*
A$:US$	**New**	**0.72**	**0.75**	**0.75**	**0.74**	**0.74**
	Old	*0.70*	*0.75*	*0.75*	*0.75*	*0.75*
	Chng	*3%*	*0%*	*0%*	*-1%*	*-1%*

Source: Foster Stockbroking estimates.

Tight markets lifting prices

- A number of producers have reported price increases for zircon, rutile, and ilmenite progressively this year, with major increases in the latter part of the year.
- **Zircon premium spot still above our forecasts**
  - Zircon has incurred the largest increases. Spot price of zircon premium is US$2,235/t up from US$1,335/t at beginning of year (Bloomberg).
  - Pyx Mining (PYX) has reported a US$555/t increase for its zircon premium from September, following earlier rises in March, May, and June.
  - Base Resources (BSE) reported a US$600/t increase for its zircon in the December quarter, following US$150/t increase in the September quarter.
  - Iluka Resources (ILU) increased its zircon (premium and standard) price US$70/t in April, US$125/t in July, and most recently US$120-170/t in October this year.
- **Rutile**
  - ILU has stated all major rutile producers have increased prices US$175-US$200/t for the December quarter.

Demand lifts while supply is tight

- Miners, as well as industry intelligence body TZMI, have reported that zircon demand has risen across China, India, South America, and Europe, with increasing tile production as the global economy recovers.
- Strong pigment demand, especially from China, is feeding rutile and ilmenite demand, while we expect the US infrastructure package should also be positive.
- The lack of new oncoming supply is keeping the market tight. ILU has stated customers have low inventories, while both disruptions to, and uncertainty surrounding, supply from Richards Bay and Sierra Rutile maintain price tension.

EARNINGS FORECASTS

Upgrade on higher prices

- We have upgraded STA earnings on higher prices for all its minerals sand products. FY23e NPAT rises to $1M from a -$9M loss, while for the first full year of production – FY24e – NPAT rises 40% to $63M from $40M.

Forecast Coburn EBITDA $110M vs $91M previously

- We now forecast $110M Coburn EBITDA in its first year of full production capacity in FY24e, which is up 21% from our prior $91M forecast.
- Our forecast revenue/C1 cost ratio rises to 2.5x from 2.3x.

Figure 3: STA Earnings Forecasts - Changes

	FY22e			FY23e			FY24e		
	New	**Old**	**Chng**	**New**	**Old**	**Chng**	**New**	**Old**	**Chng**
Coburn	0	*0*	*0%*	50	*45*	*11%*	203	*178*	*14%*
Tanzania	0	*0*	*0%*	0	*0*	*0%*	0	*0*	*0%*
Sales	**0**	***0***	***0%***	**50**	***45***	***11%***	**203**	***178***	***14%***
Operating costs	7	*14*	*-50%*	31	*37*	*-17%*	101	*103*	*-1%*
Coburn	0	*0*	*0%*	27	*23*	*18%*	110	*91*	*21%*
Tanzania	0	*0*	*0%*	0	*0*	*0%*	0	*0*	*0%*
Corp & expln	-7	*-14*	*-50%*	-8	*-15*	*-47%*	-9	*-16*	*-44%*
EBITDA	**-7**	***-14***	***-50%***	**19**	***7***	***174%***	**101**	***75***	***35%***
D&A	0	*0*	*0%*	3	*3*	*0%*	12	*12*	*0%*
Coburn	0	*0*	*0%*	24	*20*	*21%*	98	*79*	*24%*
Tanzania	0	*0*	*0%*	0	*0*	*0%*	0	*0*	*0%*
Corp & expln	-7	*-14*	*-50%*	-8	*-15*	*-46%*	-9	*-16*	*-43%*
EBIT	**-7**	***-14***	***-50%***	**16**	***5***	***224%***	**89**	***63***	***41%***
Net interest exp	8	*-2*	*nm*	14	*14*	*0%*	16	*16*	*0%*
PBT	-15	*-12*	*22%*	2	*-9*	*-121%*	73	*47*	*55%*
Tax	0	*0*	*0%*	1	*0*	*nm*	10	*2*	*nm*
NPAT adj.	**-15**	***-12***	***nm***	**1**	***-9***	***nm***	**63**	***45***	***40%***
NRI	0	*0*	*0%*	0	*0*	*0%*	0	*0*	*0%*
NPAT reported	**-15**	***-12***	***nm***	**1**	***-9***	***nm***	**63**	***45***	***40%***

Source: Foster Stockbroking estimates.

STA VALUATION

Increases to $0.62 risked (prior $0.52)

- Our risked share valuation (0.8x NPV_{10}) of STA increases to $0.62 from $0.52 due to our higher price forecasts. This has lifted not only our Coburn valuation, but that of Fungoni and Tajiri. Our unrisked valuation (1.0x NPV_{10}) is now $0.78 (prior $0.64).

Figure 4: STA Valuation, nominal 10% WACC

Segment	Unrisked A$M	A$/share	Risked A$M	A$/share	1-Risk Factor
Coburn Reserves	496	$0.44	471	$0.41	95%
Coburn Expansion	112	$0.10	84	$0.07	75%
Fungoni (84%)	32	$0.03	21	$0.02	65%
Tajiri (84%)	205	$0.18	103	$0.09	50%
Corporate	-51	-$0.04	-48	-$0.04	95%
Other Tanzania exploration	15	$0.01	5	$0.00	30%
Net cash (debt) end Sep 2021	71	$0.06	71	$0.06	100%
Cash from in money options	2	$0.00	2	$0.00	95%
Total	**883**	**$0.78**	**709**	**$0.62**	**80%**

Shares now M	1,120
Performance rights M	8
Options-in-money at valuation M	11
Fully diluted shares M	**1,139**

Source: Foster Stockbroking estimates.

Spot zircon case

- We note running STA at spot zircon price of US$2,235/t yields a risked valuation of $0.92, while FY24e earnings would yield Coburn EBITDA of $151M, and STA EBITDA $142M and NPAT $91M.

MAINTAIN BUY, 12-MONTH PT $0.62 (PRIOR $0.52)

- We maintain our Buy, increasing our 12-month price target to $0.62 from $0.52, based on our risked valuation (0.8x NPV_{10}). Share price catalysts include:

  1) Further progress on Coburn project construction;

  2) Coburn Resource and Reserves upgrades;

  3) Finalisation of Framework Agreement for Tanzanian projects; and

  4) Higher mineral sands prices.

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