Nickel Mines Poised For Price Recovery

Jul 10, 2020

A spotlight has fallen on Nickel Mines (the company) after having completed the acquisition of a further stake in its Indonesian projects. Shaw and Partners initiates coverage.

-Economic interest in Morowali projects raised to 80%
-Catalysts include improving nickel price
-Commencement of dividends considered likely in 2021

By Eva Brocklehurst

Electric vehicles hold the promise of increased demand for nickel as a cathode in batteries, which brings Nickel Mines ((NIC)) into the spotlight. Shaw and Partners highlights that having started out as an explorer, Nickel Mines is now more an industrial producer than a mining company.

Nickel pig iron is being produced from rotary kiln electric furnaces (RKEF) in the Indonesian Morowali Industrial Park in partnership with stainless steel producer Tsingshan, the world's largest, which is also a strategic shareholder in Nickel Mines.

Tsingshan has pioneered the use of RKEF to produce molten pig iron, and invested substantially in the development of the Indonesian industry. There are two nickel production projects, in which Nickel Mines recently increased its economic interest to 80% from 60%, funded by an entitlement offer.

Bell Potter asserts this was a major milestone and the projects should be strongly accretive, justifying the US$120m cost. The stock is considered a top pick and the broker retains a Buy rating with a $1.08 target. Macquarie also anticipates increased ownership, which came six months earlier than expected, and will raise the company's production share to 36,000tpa. Macquarie maintains an Outperform rating with a $0.90 target.

Indonesian Projects

Hengjaya started in early 2019 and Ranger in mid 2019. Both are now producing 21,000tpa of nickel each at a cost of around US$7,750/t. **Nickel Mines has a 33-34,000tpa share in this production, making it the largest pure exposure to nickel on the ASX**.

Shaw and Partners acknowledges some investors may be concerned about the operations in Indonesia and the partnership with a Chinese company, as well as the fact there are both Indonesian and Chinese strategic stakeholders.

However, Nickel Mines is not an outsider, the relationships are strong and Tsingshan has an 18% stake in Nickel Mines. Moreover, at a mid-cycle nickel price of US$6.50/lb the two projects are expected to generate a combined free cash flow of around US$210m per annum.

Shaw has initiated coverage of the stock with a Buy rating and $1.04 target, noting catalysts include the ongoing stability of operations and improvement in the nickel price from its cyclical lows as well as the commencement of dividend payments, considered likely in 2021.

Given the increased use of electric vehicles, Shaw expects the price of nickel will increase around 30% from the current spot price , to an incentive price of around US$7.50/lb once the pandemic-related shocks abate.

The broker acknowledges risk lies with volatile and often arbitrary policy changes in Indonesia, such as the ban on exporting unprocessed ore, and as a result the nickel price is difficult to forecast.

The looming export ban drove the nickel market in 2019 and it was intended to stimulate domestic processing of ore and produce value-added nickel products. Fortunately, as Shaw notes, Tsingshan was an early mover and began construction of nickel pig iron and steel making facilities in Indonesia ahead of the bans.

Nickel Mines listed on the ASX in 2018 at $0.35 a share and has an 80% stake in the Hengjaya mine, a high-grade, long-life nickel laterite deposit in central Sulawesi, not far from the Morowali projects. The balance is owned by its local Indonesian partner. The mine produces direct shipping ore and the bulk is sold to the Morowali facilities for the production of nickel pig iron.