

Nickel Mines (NIC)

Rating: Buy | Risk: High | Price Target: \$1.08

1H20 result – cash flowing and maiden dividend declared

Key Information

Current Price (\$ps)	0.68
12m Target Price (\$ps)	1.08
52 Week Range (\$ps)	0.25 - 0.68
Target Price Upside (%)	58.2%
TSR (%)	58.2%
Reporting Currency	USD
Market Cap (\$m)	1,133
Sector	Materials
Avg Daily Volume (m)	4.1
ASX 200 Weight (%)	0.06%

Fundamentals

YE 31 Dec (USD)	FY19A	FY20E	FY21E	FY22E
Sales (\$m)	236	484	674	682
NPAT (\$m)	57	75	235	212
EPS (cps)	3.5	4.0	11.0	10.0
EPS Growth (%)	(42.3%)	12.1%	177.6%	(9.6%)
DPS (cps) (AUD)	0.0	0.0	8.2	9.5
Franking (%)	0%	0%	0%	0%

Ratios

YE 31 Dec	FY19A	FY20E	FY21E	FY22E
P/E (x)	13.0	12.6	4.5	5.0
EV/EBITDA (x)	8.1	5.8	2.6	2.6
Div Yield (%)	0.0%	0.0%	12.0%	14.0%
Payout Ratio (%)	0.0%	0.0%	54.4%	70.2%

Price Performance

YE 31 Dec	1 Mth	2 Mth	3 Mth	1 Yr
Relative (%)	15.4%	17.7%	31.3%	40.4%
Absolute (%)	17.9%	20.7%	36.8%	32.4%
Benchmark (%)	2.5%	3.0%	5.5%	(8.0%)



Price performance indexed to 100

Source:

Major Shareholders

Shanghai Decent (Tsingshan)	18.6%
PT Karunia Bara Perkasa	16.1%
BlackRock Investment Management (UK) Ltd	6.5%
Norm Seckold	5.8%
Shanghai Wanlu	5.7%

Event

Nickel Mines has reported underlying 1H20 NPAT up 188% to US\$46m and has also declared a maiden 1cps dividend.

Highlights

- Nickel Mines has an 80% economic interest in two Rotary Kiln Electric Furnace (RKEF) projects in the Indonesia Morowali Industrial Park (IMIP). The Chinese steel company Tsingshan holds the other 20%. The Hengjaya project started in early-2019 and Ranger in mid-2019. Both projects have now reached steady state operation and are each producing ~21ktpa nickel (100% basis) at a cost of ~US\$7,500/t. Nickel Mines share totals 33-34ktpa which makes the company the largest pure play nickel exposure on the ASX.
- The strong year-on-year comparisons reflect the first full period of production from both the Ranger and Hengjaya RKEF projects. Earnings are likely to increase again with ownership increasing to 80% this half (from 60%) and with the nickel price strengthening above US\$15,000/t.
- The nickel market is tightening with Chinese imports of stainless steel and nickel pig iron (NPI) surging in July. Chinese stainless steel imports are up 444% yoy to 141kt in July and NPI up 74%. The increase is largely due to the Indonesia nickel ore export bans, and the subsequent relocation of Chinese stainless steel and NPI production to Indonesia, of which Tsingshan is the major player and in which Nickel Mines is integrally involved.
- Earlier this year the company exercised its option to increase its stake in the two RKEFs from 60% to 80% and fully funded this via an equity raise of A\$231m. This was a surprisingly conservative approach given the strength of the balance sheet and cash flow, but does position Nickel Mines to acquire additional assets in the IMIP over the next 1-2 years.
- We also note that repatriation of funds from the RKEF projects to shareholders commenced in the half. Nickel Mines received cash payments of US\$25m from Hengjaya and US\$11m from Ranger.

Nickel Mines 1H20 result (US\$m)	1H20	1H19	Change
Revenue	228	57	300%
EBITDA	56	10	460%
Underlying NPAT	46	16	188%
Cash flow from operations	79	38	108%
Capex	5	30	-83%
Free cash flow	74	8	825%
Net cash	46	50	-8%
Dividend (cps)	1	0	n/a

Recommendation

We retain our Buy recommendation and lift our price target from A\$1.04ps to \$1.08ps. Catalysts for the stock to reach our price target include;

- Ongoing stability of operations now that both the Hengjaya and Ranger RKEF projects have reached steady state.
- Improvements in the nickel price from cyclical lows.
- Investments in additional RKEF capacity in the IMIP.

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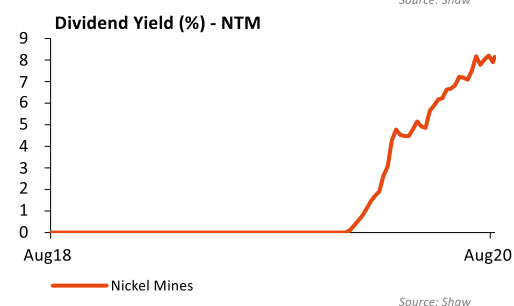
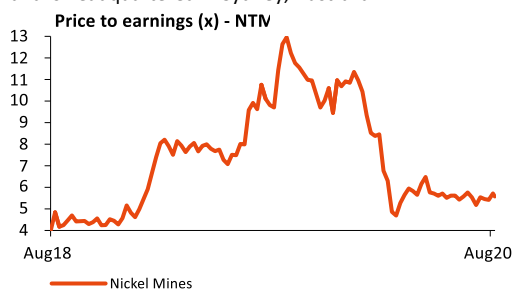
**Nickel Mines
Materials
Materials**

FactSet: NIC-AU / Bloomberg: NIC AU

Key Items	Data
Recommendation	BUY
Risk	HIGH
Price (\$ps)	0.68
Target Price (\$ps)	1.08
52 Week Range (\$ps)	0.25 - 0.68
Shares on Issue (m)	1,665
Market Cap (\$m)	1,133
Enterprise Value (\$m)	1,066
TSR (%)	58.2%

Company Description

Nickel Mines Ltd. is a nickel producer with assets in Indonesia and operates in partnership with Tsingshan, the world's largest stainless steel producer. Nickel Mines produces nickel ore from the Hengjaya Mine which supplies feedstock to the Indonesia Morowali Industrial Park (IMIP). The company's main asset is an 80% stake in the Hengjaya and Ranger rotary kiln electric furnaces (RKEF) located in IMIP. The company was founded on September 12, 2007 and is headquartered in Sydney, Australia.



Financial Year End: 31 December

Investment Summary (USD)	FY19A	FY19A	FY20E	FY21E	FY22E
EPS (Reported) (cps)	6.1	3.5	4.0	11.0	10.0
EPS (Underlying) (cps)	6.1	3.5	4.0	11.0	10.0
EPS (Underlying) Growth (%)	n/a	(42.3%)	12.1%	177.6%	(9.6%)
PE (Underlying) (x)	4.7	13.0	12.6	4.5	5.0
EV / EBIT (x)	57.8	9.7	7.4	2.8	2.9
EV / EBITDA (x)	38.5	8.1	5.8	2.6	2.6
DPS (cps) (AUD)	0.0	0.0	0.0	8.2	9.5
Dividend Yield (%)	0.0%	0.0%	0.0%	12.0%	14.0%
Franking (%)	0%	0%	0%	0%	0%
Payout Ratio (%)	0.0%	0.0%	0.0%	54.4%	70.2%
Profit and Loss (USD) (m)	FY19A	FY19A	FY20E	FY21E	FY22E
Sales	65	236	484	674	682
Sales Growth (%)	n/a	263.5%	105.2%	39.2%	1.1%
Other Operating Income	3	1	1	1	1
EBITDA	20	97	136	307	304
EBITDA Margin (%)	31.5%	41.2%	28.1%	45.5%	44.6%
Depreciation & Amortisation	(7)	(16)	(30)	(30)	(30)
EBIT	14	81	106	277	274
EBIT Margin (%)	21.0%	34.2%	21.9%	41.1%	40.2%
Net Interest	58	11	(5)	(3)	4
Pretax Profit	72	91	101	274	279
Minorities	6	35	26	39	39
NPAT Underlying	66	57	75	235	212
Significant Items	0	0	0	0	0
NPAT Reported	66	57	75	235	212
Cashflow (USD) (m)	FY19A	FY19A	FY20E	FY21E	FY22E
EBIT	14	81	106	277	274
Payments to Suppliers	(28)	(170)	(349)	(368)	(378)
Receipts from Customers	33	213	485	675	683
Tax Paid	(1)	(5)	0	0	0
Net Interest	0	0	0	2	8
Depreciation & Amortisation	0	0	0	0	0
Other	0	0	(8)	(10)	1
Operating Cashflow	4	38	129	299	313
Capex	(20)	(30)	(13)	(3)	(3)
Acquisitions and Investments	(120)	(1)	(150)	0	0
Disposal of Fixed Assets/Investments	10	7	0	0	0
Other	(11)	0	0	0	0
Investing Cashflow	(141)	(24)	(163)	(3)	(3)
Equity Raised / Bought Back	173	(0)	150	0	0
Dividends Paid	0	0	0	(43)	(149)
Change in Debt	(2)	(30)	0	(30)	(35)
Other	15	17	(5)	(5)	(3)
Financing Cashflow	186	(13)	145	(77)	(187)
Exchange Rate Effect	(1)	(0)	0	0	0
Net Change in Cash	48	1	111	219	123
Balance Sheet (USD) (m)	FY19A	FY19A	FY20E	FY21E	FY22E
Cash	49	50	161	379	502
Accounts Receivable	44	97	126	129	131
Inventory	9	56	115	129	131
Other Current Assets	7	1	1	1	1
PPE	340	629	732	705	678
Total Assets	532	897	1,229	1,438	1,537
Accounts Payable	42	52	133	140	144
Short Term Debt	4	4	4	4	0
Long Term Debt	0	61	61	31	0
Income Taxes Payable	0	1	1	1	1
Other	30	57	57	58	85
Total Liabilities	77	175	256	234	230
Total Shareholder Equity	455	722	973	1,205	1,307
Ratios	FY19A	FY19A	FY20E	FY21E	FY22E
ROE (%)	n/a	15.3%	14.0%	31.3%	24.2%
Gearing (%)	(16.8%)	3.4%	(17.2%)	(68.8%)	(123.8%)
Net Debt / EBITDA (x)	(2.2)	0.2	(0.7)	(1.1)	(1.7)

Key risks

- The nickel price is volatile and is often driven by arbitrary policy changes such as the Indonesian export ban. As such, the price of nickel is relatively difficult to forecast and the actual price may differ substantially from our forecasts.
- Some investors may be concerned that the company operates in Indonesia, in partnership with a Chinese company and with Indonesian and Chinese strategic shareholders. However, Nickel Mines is 'inside the fence' and not an outsider. The relationship with Tsingshan is strong, and Tsingshan has a strong relationship with Indonesian authorities.
- Smaller companies carry more significant 'key personnel' risk than larger organisations. If senior management depart the company, then it could delay projects or exacerbate operational risks.

Core drivers and catalyst

- Nickel is predominantly used in the production of stainless steel (69% of consumption) but is finding growing use as a cathode in lithium ion batteries. The electrification of light vehicles is likely to see increased demand for nickel. Consensus forecasts expect the nickel price to increase ~30% from today's spot price at US\$5.90/lb to an incentive price of ~US\$7.50/lb once the COVID-19 demand shocks abate. We agree.
- Nickel Mines has an 80% economic interest in two RKEF projects in the IMIP. Even at current low nickel prices of ~US\$5.90/lb the projects are strongly free cash flow positive (US\$160mpa, 100% basis combined). At a mid-cycle nickel price of US\$6.50/lb, the two projects will generate combined free cash flow of about US\$210mpa (100% basis).
- We value each RKEF project at US\$947m (100%, NPV @ 11%) and Nickel Mines recently exercised an option to increase its economic interest from 60% to 80% in both projects for US\$120m.
- At spot nickel prices (US\$5.90/lb), Nickel Mines is trading on a PE multiple of just 7.6x and an EV/EBITDA multiple of 4.5x. At mid-cycle nickel prices of US\$6.50/lb these multiples drop to 5.4x PE and 3.3x EV/EBITDA. If nickel lifts to US\$7.50/lb, as we expect, then the multiples reduce to 3.7x PE and 2.3x EV/EBITDA.

Rating Classification

Buy	Expected to outperform the overall market
Hold	Expected to perform in line with the overall market
Sell	Expected to underperform the overall market
Not Rated	Shaw has issued a factual note on the company but does not have a recommendation

Risk Rating

High	Higher risk than the overall market – investors should be aware this stock may be speculative
Medium	Risk broadly in line with the overall market
Low	Lower risk than the overall market

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