

# AMERICAN PACIFIC BORATES (ABR)

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## Start Your Engines

### KEY POINTS

- **ABR has received the Underground Injection Control (UIC) permit for the Fort Cady project in California.** The delay in the receipt of this vital Government permit had been a major handbrake on the development of the Fort Cady project and viewed as a significant investment risk.
- **Phase 1A is now fully funded.** The issue of the permit will now trigger (pending shareholder approval) the \$US30m convertible note previously agreed to with Virtova Capital Management. In addition to the con note, ABR recently raised \$31.8m through the issue of 53m shares at \$0.60/sh. Phase 1A capex of US\$50.3m is now fully funded with detailed engineering now being accelerated and construction activities ramping up on site. Phase 1A will produce 8ktpa of boric acid and 36.3ktpa of SOP with first production on track for Q3 CY2021.
- **New Chairman appointed.** Mr David Salisbury has been appointed Chairman following the retirement of Harold (Roy) Shipes. Mr Salisbury has over 40 years' experience in the resources industry specifically in building and operating mining projects in the United States.

### INVESTMENT VIEW

The ABR story continues to gather momentum with issue of the final major permit a significant de-risk event. With Phase 1A fully funded, ABR is now on the path to production.

We like the Fort Cady project and the intelligent approach to mining and self-producing the largest input cost, being hydrochloric acid (HCl). HCl can be produced via a traditional Mannheim process, which converts a Muriate of Potash (MOP) product to a premium SOP product which is in high demand as a fertilizer, especially on chloride sensitive crops such as Avocado, citrus, and potatoes. Through geographical good fortune, the Fort Cady project is located close to the Californian agricultural industry which is responsible for >30% of the current SOP demand in the United States. Through the sale of SOP as a by-product, the cost of production for a tonne of boric acid is actually negative once the project is in full production, with an expected total opex cost of -US\$19.96/boric acid tonne.

We maintain our view that ABR offers a compelling investment opportunity with DFS financials unlike any other resource project you will find today. Project construction has been staged to reduce total capital exposure, and we expect positive operational cashflows by FY24 and estimate EBITDA margins exceeding US\$100m by FY25. We re-run our DCF model considering this reduced project/financing risk. **We upgrade our recommendation to BUY (previous speculative buy) and our price target to \$1.76 (previous \$1.28/sh).**

### NEAR TERM CATALYSTS

**Construction Progress** – ABR is now in construction/development phase with progress updates on time and budget milestones.

**Marketing and Sales Strategy** – We are unlikely to see offtake contracts for Phase 1A given the low production volumes, however more clarity around the marketing strategy and commodity pricing should filter through until commissioning.

**Phase 1B Financing** – Phase 1B requires an additional US\$156m. Phase 1B is expected to commence construction during CY2022, however may be accelerated if sufficient progress is made on Phase 1A.

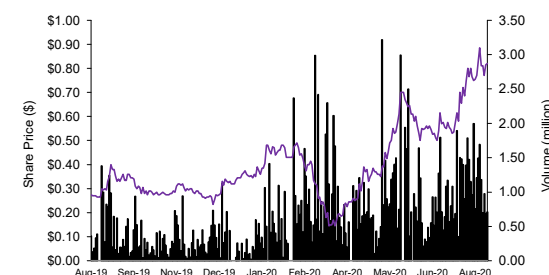
Recommendation	BUY
Previous Recommendation	Speculative Buy
Risk Rating	High
Current Share Price	\$0.82
12 Month Price Target	\$1.76
Total Return (Capital + Yield)	114.6%
Market Capitalisation	\$260.5m
Liquidity	\$6.3m/month

### Financial Forecasts & Valuation Metrics

Y/e June (\$m)	2020F	2021F	2022F	2023F
Revenue	0.1	0.1	42.8	42.8
EBITDA	(2.4)	(4.9)	7.8	7.1
NPAT	(2.6)	(4.6)	(2.2)	(2.0)
EPS (cps)	(0.8)	(1.2)	0.5	0.5
EPS Growth %	na	na	na	na
EV / EBITDA (x)	(58.5)	(50.7)	31.1	64.0
PER (x)	(70.0)	(48.0)	106.7	126.6
Dividend Yield	0.0	0.0	0.0	0.0

Source: PAC Partners estimates

### 12 Month Relative Share Price Performance



Source: IRESS

### Risks

**Development Risk:** ABR is now entering construction phase and carries normal construction/development risk including cost/time overruns and other operational issues.

**Access to Capital:** ABR require further capital to fund future construction /development phases. There is no certainty that capital will become available to ABR at satisfactory commercial terms.

**Commodity Price Risk:** As with all resource projects, geopolitical risks, competitive forces, and changes in commodity application with technological improvements could see demand and or prices for ABR focused commodities be reduced. Further, boric acid and SOP have no transparent spot markets and being a new entrant to both commodities, there is no guarantee ABR will achieve stated revenues or sales volumes.

**DISCLOSURE:** PAC Partners was Joint Lead Manager to the May 2020 placement and received fees on commercial terms for these services. The information contained in this report is provided by PAC Partners to Wholesale Investors only.

The information contained in this report is to be read in conjunction with other important disclosures at the end of this document.

## COMPANY OVERVIEW

American Pacific Borates Limited (ABR) own the Fort Cady borate/SOP project in California, United States. The Fort Cady Project is located in the Mojave Desert in the County of San Bernardino and has the largest known contained borate occurrence in the world not owned by the two dominant borate producers being Rio Tinto Limited (RIO) and Eti Maden which account for approximately 80% of the global 3.8mtpa boric acid equivalent market. ABR's planned production will account for approximately 2% of global demand during the initial operations, climbing to approximately 6% at full production.

ABR intend to extract boric acid from the project as the primary commodity with by-product credits attributable to the production and sale of sulphate of potash (SOP), hydrochloric acid (HCl) (during the initial phases) and gypsum. Gypsum will be produced directly from the boric acid processing facility, while SOP and HCl will be produced from a separate Manheim facility on site.

The project has been split into four phases to ease cashflow and financing risk. Full production of all four phases is expected in 2027/28.

**Figure 1: Key Financial Metrics**

<b>Fort Cady Project (Boric Acid and SOP Production)</b>	
<b>Phase 1A Only</b>	
Capex	US\$50.3 million
NPV <sub>8</sub>	US\$224.3 million
IRR	35.9%
EBITDA in first full year of production	US\$19.6 million
<b>Phase 1A &amp; 1B Only</b>	
Capex (Phase 1B only)	US\$156.0 million
NPV <sub>8</sub>	US\$773.8 million
IRR	32.4%
EBITDA in first full year of production	US\$73.2 million
<b>Phase 1 &amp; 2 Only</b>	
Capex (Phase 2 only)	US\$268.3 million
NPV <sub>8</sub>	US\$1.709 billion
IRR	37.8%
EBITDA in first full year of production	US\$242.2 million
<b>Full Project (Phases 1, 2, &amp; 3)</b>	
Capex (Phase 3 only)	US\$263.2 million
NPV <sub>8</sub>	US\$1.965 billion
IRR	39.4%
EBITDA in first full year of production	US\$438.4 million

Source: ABR

## PERMIT APPROVAL, PROJECT FINANCING AND CONSTRUCTION

The Underground Injection Control (UIC) permit has now been issued to ABR for the initial phase of the Fort Cady project. The issue of this permit has been a major handbrake on the development of the Fort Cady project and viewed as a significant investment risk.

ABR had previously agreed to a binding term sheet with Virtova Capital Management for a US\$30m convertible note subject to the grant of the UIC permit and shareholder approval. The convertible note has a term of 24 months at an interest rate of 11.6%pa. Conversion is at the investors election to a total of 51,282,050 shares at a headline price of \$1.00/sh. (assuming an exchange rate of 0.65) In addition to the convertible note, ABR raised AUD\$31.8m through a placement of 53m shares at \$0.60/sh in May 2020. ABR is now fully funded to meet the expected \$US50.3m in capex to build Phase 1A of the Fort Cady project.

Construction activities are now ramping up on site with the delivery of critical infrastructure, establishment of water supply and other site access works ongoing. Detailed engineering is now being fast tracked with a view of initial commissioning of the project in Q2 CY21 and production commencing in the second half of CY21.

**Figure 2: Fin Fan Cooler Delivered to Site**



Source: ABR

**VALUATION**

Given the UIC permit has been granted and Phase 1A has been fully funded, we see significantly less risk in Fort Cady entering production. We remodel our cashflows based on previous operating and commodity assumptions. We reduce our WACC to 10% (previous 12%) and factor in a 30% risk discount factor (previous 50%). We have assumed the convertible note is fully converted to shares and allow further capital raises to fund future capex requirements at 90/10 debt/equity. We estimate a total of 464m shares are issued prior to FY26. We believe we remain conservative on our valuation estimates and are considerably more cautious than the Company’s own PFS. We still see risk in commodity pricing/volumes, being a new entrant to both the boric acid and SOP markets. Even factoring in our conservative view, we see considerable value in ABR at current levels. We value ABR at \$1.76/sh, representing 115% upside to the current price.

**Figure 3: ABR DCF Valuation**

Valuation	\$m	\$/sh
Phase 1A&B	\$186.1	\$0.40
Phase 2	\$398.3	\$0.86
Phase 3	\$269.3	\$0.58
Corporate	-\$75.4	-\$0.16
Cash/Debt	\$38.7	\$0.08
<b>Total</b>	<b>\$817.1</b>	<b>\$1.76</b>

Source: PAC Partners

We sense check our valuation by determining the PV of the ABR PFS financials (Figure 4). Using Compass Minerals (CMP.NYS) as a benchmark, recently trading on an EV/EBITDA multiple of 7.7 - 8.4 x we estimate the PV of the 2028 (being the first full year of production) US\$438.4m EBITDA to be AUD \$904m, implying a fully diluted valuation of \$1.95/sh.

**Figure 4: EV/EBITDA Valuation Based on ABR PFS**

EV/EBITDA Valuation	AUD \$m
EBITDA 2028 (ABR PFS)	\$626
EV/EBITDA Multiple x	8.0x
Implied EV	\$5,010
Time Discount Factor	0.47x
EV	\$2,337
Capex (undiscounted)	-\$1,054
Less 30% Risk	-\$385
Cash	\$38.7
Corporate	-\$33
<b>Implied Equity Value</b>	<b>\$904</b>
<b>Implied \$/Sh</b>	<b>\$1.95</b>

Source: PAC Partners

## INVESTMENT VIEW

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We like the Fort Cady project and the intelligent approach to mining and self-producing the largest input cost, being hydrochloric acid (HCl). HCl can be produced via a traditional Manheim process, which converts a Muriate of Potash (MOP) product to a premium SOP product which is in high demand as a fertilizer, especially on chloride sensitive crops such as Avocado, citrus, and potatoes. Through geographical good fortune, the Fort Cady project is located close to the Californian agricultural industry which is responsible for >30% of the current SOP demand in the United States. Through the sale of SOP as a by-product, the cost of production for a tonne of boric acid is actually negative once the project is in full production, with an expected total opex cost of -US\$19.96/boric acid tonne.

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## UPCOMING CATALYSTS

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**Marketing and Sales Strategy** – We are unlikely to see offtake contracts for Phase 1A given the low production volumes, however more clarity around the marketing strategy and commodity pricing should filter through until commissioning.

**Phase 1B Financing** – Phase 1B requires an additional US\$156m. Phase 1B is expected to commence construction during CY2022, however may be accelerated if sufficient progress is made on Phase 1A. Phase 2 (Capex US\$268.3m) may also be accelerated subject to the performance of Phase 1A.

## RISKS

**Emerging companies are usually subject to normal key person and funding risks.**

### Access to Capital

ABR require further capital to fund future construction /development phases. There is no certainty that capital will become available to ABR at satisfactory commercial terms.

## Development Risk

ABR is now entering construction phase and carries normal construction/development risk including cost/time overruns and other operational issues.

## Commodity pricing and demand

As with all resource projects, geopolitical risks, competitive forces, and changes in commodity application with technological improvements could see demand and or prices for ABR focused commodities be reduced. Further, boric acid and SOP have no transparent spot markets and being a new entrant to both commodities, there is no guarantee ABR will achieve stated revenues or sales volumes.

### American Pacific Borates Limited

ABR.AX

16/08/2020

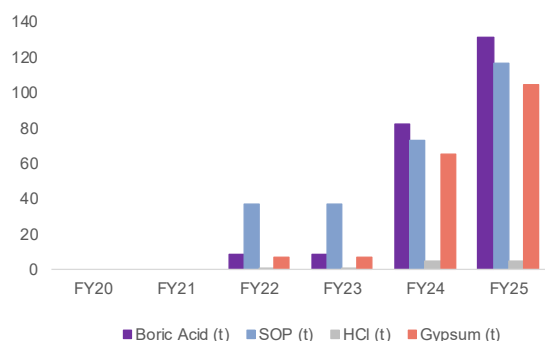
#### Price Information

Price (\$/Share)	\$0.82
Mkt Cap (\$m) (dil)	\$260.5
Enterprise Value (\$m)	\$221.7
Target Price (\$/Share)	\$1.76
Recommendation	BUY
Total Return	114.6%

#### Commodity/FX Forecasts

	FY20	FY21	FY22	FY23
Boric Acid (US\$/t)	\$750	\$750	\$750	\$750
SOP (US\$/t)	\$650	\$650	\$650	\$650
HCl (US\$/t)	\$165	\$165	\$165	\$165
Gypsum (US\$/t)	\$33	\$33	\$33	\$33
AUD:USD	0.70	0.70	0.70	0.70

#### Production Summary '000 tonnes



#### Valuation (fully diluted)

	A\$m	Per Share
Phase 1A&B	\$186.1	\$0.40
Phase 2	\$398.3	\$0.86
Phase 3	\$269.3	\$0.58
Corporate	-\$75.4	-\$0.16
Cash	\$38.7	\$0.08
<b>Total</b>	<b>\$817.1</b>	<b>\$1.76</b>

#### Resources & Reserves

	Tonnes (m)	B <sub>2</sub> O <sub>3</sub> %	B <sub>2</sub> O <sub>3</sub> (mt)
<b>Reserves</b>			
Fort Caddy	41.0	6.6%	2.7
<b>Total</b>	<b>41.0</b>	<b>6.6%</b>	<b>2.7</b>
<b>Resources</b>			
Fort Caddy	120.4	6.5%	7.8
<b>Total</b>	<b>120.4</b>	<b>6.5%</b>	<b>7.8</b>

Year End - Jun	FY20F	FY21F	FY22F	FY23F	FY23F
<b>KEY METRICS</b>					
EPS Growth (%)	na	na	na	(15.7)	1,975.8
PER (x)	(70.0)	(48.0)	106.7	126.6	6.1
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0
EV/EBITDA (x)	(58.5)	(50.7)	31.1	64.0	4.8
EV (\$m)	202.1	354.7	348.4	648.2	611.9
ROE (%)	(5.1)	(5.9)	2.3	1.6	25.3
ROA (%)	(5.0)	(4.6)	1.6	0.7	10.1
ROIC (%)	(3.3)	(3.9)	3.5	1.1	19.3

#### PROFIT & LOSS

Revenue	0.1	0.1	42.8	42.8	160.9
EBITDA	(2.4)	(4.9)	7.8	7.1	89.3
Depreciation & Amortisation	(0.0)	(0.0)	(2.7)	(2.8)	(10.8)
EBIT	(2.4)	(4.9)	5.1	4.3	78.5
Net Interest Expense	(0.1)	0.3	(2.9)	(2.3)	(17.1)
Income Tax	0.0	0.0	0.0	0.0	(19.0)
NPAT Reported	(2.6)	(4.6)	2.2	2.0	42.4
NPAT Adjusted	(2.6)	(4.6)	2.2	2.0	42.4

#### PER SHARE DATA

Shares on Issue (m)	313.9	382.2	406.3	439.2	450.2
EPS Reported	(0.8)	(1.2)	0.5	0.5	9.4
EPS Adjusted	(0.8)	(1.2)	0.5	0.5	9.4
DPS	0.0	0.0	0.0	0.0	0.0

#### BALANCE SHEET

Cash	38.7	13.9	26.2	52.1	46.8
Debtors & Inventory	0.6	0.5	9.9	9.9	35.8
PP&E	33.7	110.6	117.6	343.1	351.5
Intangibles	0.0	0.0	0.0	0.0	0.0
Total Assets	73.0	125.0	153.7	405.1	434.1
Borrowings	0.0	42.9	36.9	253.7	216.7
Creditors	0.3	0.0	7.0	7.0	26.4
Total Liabilities	0.3	42.9	43.9	260.8	243.2
Net Assets	72.8	82.1	109.8	144.3	190.9

#### BALANCE SHEET RATIOS

Gearing - Debt/Equity (%)	na	35.2	9.7	139.7	89.0
Interest Cover (x)	(17.4)	na	1.7	1.9	4.6
NTA per Share (cps)	0.3	0.3	0.3	0.3	0.4

#### CASH FLOW

EBITDA	(2.4)	(4.9)	7.8	7.1	89.3
Interest & Tax	(0.1)	0.3	(2.9)	(2.3)	(36.1)
Working Capital Change	(0.1)	(0.2)	(2.3)	0.0	(6.5)
Operating Cash Flow	(2.6)	(4.8)	2.6	4.8	46.7
Maintenance Capex	0.0	0.0	(2.8)	(2.9)	(14.7)
Free Cash Flow	(2.6)	(4.8)	(0.2)	1.9	31.9
Capex	(5.6)	(76.9)	(7.0)	(225.4)	(4.5)
Equity Issues	44.2	14.0	25.5	32.5	4.3
Proceeds from Borrowings	0.0	42.9	(6.0)	216.9	(37.0)
Other	(0.1)	0.0	0.0	0.0	0.0
Net Cash Flow	35.8	(24.8)	12.3	25.9	(5.3)



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## RECOMMENDATION CRITERIA

## Investment View

PAC Partners Investment View is based on an absolute 1-year total return equal to capital appreciation plus yield. A Speculative recommendation is when a company has limited experience from which to derive a fundamental investment view.

Buy	Hold	Sell
>20%	20%-5%	<5%

## Risk Rating

PAC Partners has a four tier Risk Rating System consisting of: Very High, High, Medium and Low. The Risk Rating is a subjective rating based on: Management Track Record, Forecasting Risk, Industry Risk and Financial Risk including cash flow analysis.

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- a member of the immediate family of the author of this report

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