



Resources Stocks Down Under

🗣️ *When in doubt, look intelligent.* 🗣️

- Garrison Keillor (b. 1942), American author

EVOLUTION ENERGY MINERALS

Graphite and Tanzania are both back

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Stocks Down Under rating: ★★★★★

ASX: EV1
Market cap: A\$70.4M

52-week range: A\$0.39 / A\$0.70
Share price: A\$0.435

The Perth-based Evolution Energy Minerals, developer of a graphite project in Tanzania, had a great start to its listed life in late 2021. An oversubscribed IPO raised \$22m at 20 cents per share, but the stock closed the first day, 16 November, at 62 cents. And no wonder. Graphite demand is coming back after the 2019 lows and the Definitive Feasibility Study for Evolution Energy's Chilalo Project gave it an NPV of US\$323m. With Evolution Energy stock now stabilising in the low 40s we think it's worth looking at.

Share price chart



Source: Tradingview

For a long time, it was hard to get ASX resource investors to look at any project in the East African nation of Tanzania. In July 2017 the country had, without warning, made sweeping changes to its Mining Act giving the government 16% ownership of mining projects, plus the right to acquire up to 50% of mining companies under certain conditions. Around the same time the country got into a protracted fight with Barrick (NYSE: GOLD), one of the world's largest gold miners, around unpaid taxes. So, it looked like Tanzania under President John Magufuli was no longer the investor-friendly jurisdiction it had been.

Investors like Tanzania again

Looking back, it wasn't as bad as it sounded. Magufuli's policies when it came to mining were about the same as Kevin Rudd here in Australia, who, you'll recall, proposed a mining industry super profits tax in 2010. Since 2017, various companies operating in Tanzania have now negotiated the 16% ownership arrangements and Barrick and Tanzania have made peace with each other, so it looks like Tanzania remains open for mining investment after all.

Indeed, that's the message that Mrs. Samia Suluhu Hassan, who succeeded Magufuli as President after his sudden death in March 2021, has been sending to the world lately. And that's one reason why Evolution Energy had such a great IPO last November.

We touched on Evolution Energy Minerals in Resources Stocks Down Under on [23 December 2021](#) when looking at Marvel Gold (ASX: MVL). That company, back when it was called Graphex Mining and its ASX Code was GPX, had discovered a graphite deposit in the Lindi region of southeastern Tanzania called Chilalo, about 400 km south of Tanzania's largest city, Dar es Salaam. Over the next five years, Graphex developed the project to the point where a Definitive Feasibility Study could be published (in January 2020). The company then decided there were bigger fish to fry in its gold projects in Southern Mali. But with graphite's return to favour as a commodity the decision was taken to spin Chilalo out into Evolution Energy. By that stage, something like \$21m had been spent on Chilalo. Marvel retained 31% of the spin out and the London-based ARCH Emerging Markets Partners cornerstoned the IPO via its ARCH Sustainable Resources Fund, which took 25%.

Shovel ready down in Lindi

We reckon ARCH and the other new Evolution Energy shareholders got their money's worth and then some. Chilalo is a shovel-ready and fully-permitted project with a granted Mining Licence with all the environmental approvals in place. Importantly, Chilalo has great economics. A mere US\$87.5m in capital expenditure gets you an 18-year graphite mine with an NPV of US\$331m (A\$460m) at an 8% discount rate, where the post-tax IRR is 36%. And that's only tapping part of the potential size of the mine because most of the strike at Chilalo remains undrilled. When Chilalo gets up and running it will produce around 50,000tpa of product, 30,000 of it coarse flake and concentrate and 20,000 in value-added product. The average annual EBITDA of US\$74m allows a post-tax payback period of just 3.5 years.

Large flake size

What's also attractive about Chilalo is that it's got a lot of graphite with a large flake size, meaning that the products can sell at a premium. Like, fully 58% of the resource is '+80 mesh', meaning that it is 'large', 'jumbo' or 'superjumbo' in size. The high-grade resource at Chilalo includes 20.1 million tonnes at a very high 9.9% total graphitic content (TGC) for just under 2 million tonnes of the good stuff.

The January 2020 DFS outlined three distinct graphite products for Chilalo - concentrate, expandable graphite and micronised graphite. The concentrates would sell for only about US\$1,500 a tonne versus a cost to produce of under US\$800. By contrast, expandable graphite – the kind you'd put into fire retardant applications, for example - shows an average sales price of close to US\$6,000 per tonne with only a US\$500 cost of production. And then there's micronised graphite used in things like coatings and lubricants, where the numbers are US\$2,700 to sell and US\$500 to produce. It's fair to say that margins for Chilalo will be good even in a bad year for graphite.

Evolution Energy expects to be able to make a construction decision for Chilalo by the middle of this year. 2022 will see the company do Front End Engineering Design as well as advanced studies on the downstream processing and some more exploration work on the Chilalo resource.

We believe the time is right for graphite plays on ASX because the battery minerals sector is back with a vengeance. We've all seen lithium plays do well through 2021 on the expectation that the Electric Vehicle sector will continue to expand. We expect that graphite will catch up to lithium in 2022. Throw in a return to favour of Tanzania in 2021 as well as the high valuation of Chilalo from the DFS and Evolution is well placed to succeed.

So, its four stars from us, now that the stock is stable in the low 40 cent range. Its NPV per share is \$2.84, which signals the potential upside in EV1. We believe the announcement of a Final Investment Decision for Chilalo, expected in mid-2022, is likely to be a solid share price catalyst.

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