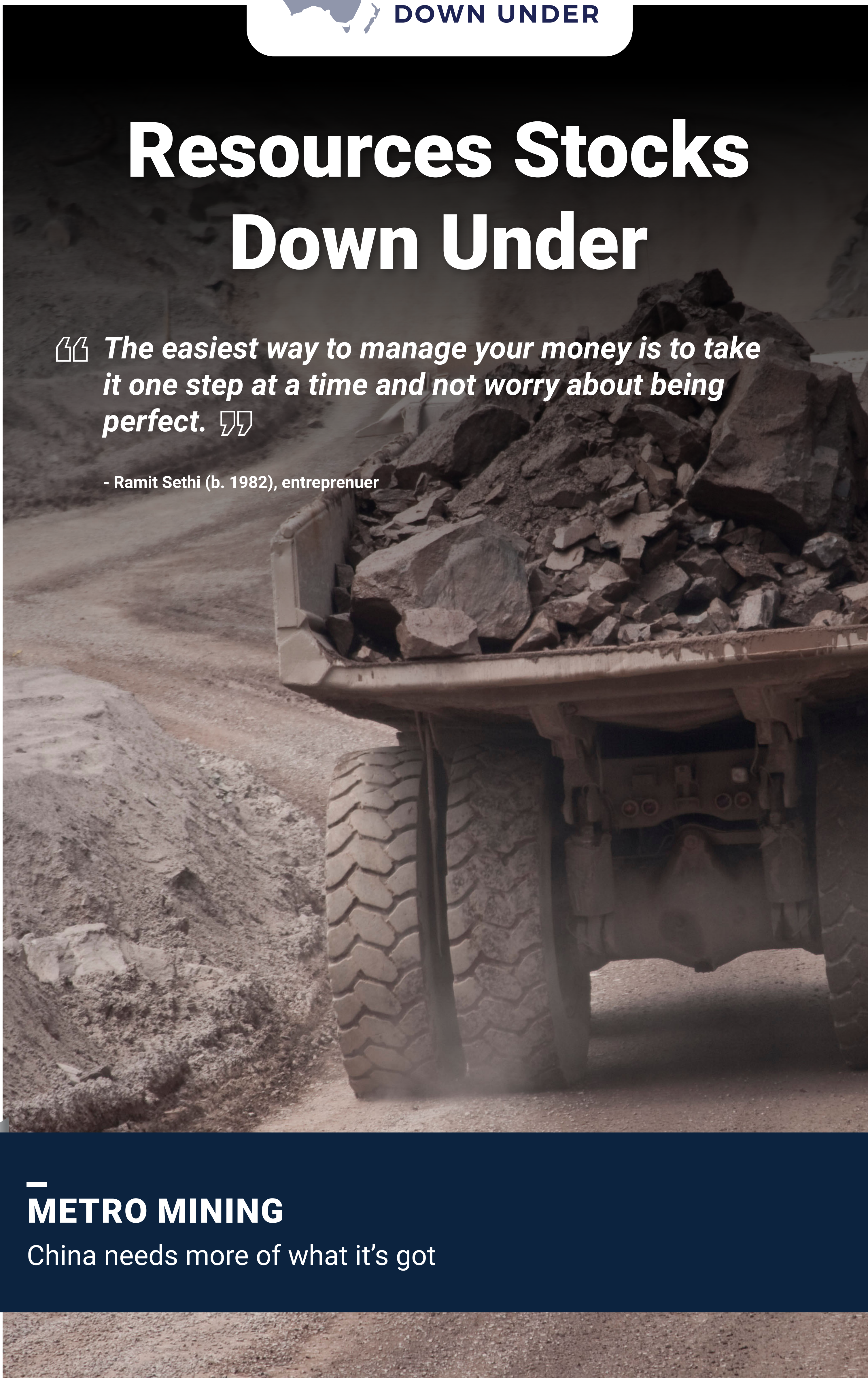
STOCKS DOWN UNDER

3 MARCH 2022



Resources Stocks Down Under

The easiest way to manage your money is to take it one step at a time and not worry about being perfect.

- Ramit Sethi (b. 1982), entrepreneur

METRO MINING

China needs more of what it's got

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Stocks Down Under rating: ★★★★

ASX: MMI
Market cap: A$83.7M

52-week range: A$0.014 / A$0.057
Share price: A$0.028

The Bauxite Hills Mine on Queensland's Cape York Peninsula, operated by Brisbane-based Metro Mining since 2018, has capacity for 4 million tonnes of the valuable red dirt. Metro Mining is now looking at ways to go to Stage 2 for Bauxite Hills, which would increase capacity to 6 million tonnes. Metro Mining stock has re-rated nicely since the August 2021 low of 1.4 cents, but it is far from valuing the Stage 2 upside, in our view.

Share price chart

Source: Tradingview

In the history of mining in Australia the port town of Weipa, on the western side of the Cape York Peninsula, holds a special place. Weipa was where large deposits of bauxite, the raw material for making alumina and aluminium, were discovered in 1955. Close to six decades after first production, Weipa continues to supply the world with high quality, but low-cost bauxite. Rio Tinto, however, no longer has the Weipa bauxite riches to itself. In 2018 a little-known company called Metro Mining brought into production a new mine 95 km to the north and called it, perhaps a little unimaginatively, Bauxite Hills. The Reserve here is 109.5 million tonnes of bauxite.

A tough three years

If you bought Metro Mining stock in April 2018 at the time of first production, you'd be badly underwater today. The stock was changing hands at 15 cents back then. Part of the trouble over the next two years related to aluminium, which declined from close to US$2,500 a tonne in April 2018 to around US1,400 a tonne at the bottom of the Corona Crash in March 2020. That decline impacted sentiment towards producers of bauxite and alumina as well the finished metal. Interestingly, bauxite hadn't moved much in price over the period. In the June 2018 quarter the price at which bauxite landed in China, as measured by the CBIX Bauxite Index, was US$48 a Dry Metric Tonne and by June 2020 it was US$45 a DMT.

However, mid-2020 weakness in bauxite pricing motivated the company to bring forward its wet-season shutdown for 2020-21. Ordinarily the wet season that far north is November to April. In 2020, Metro Mining shut down in September and bauxite was still down at around US$40/DMT by the time of the April 2021 restart.

That shutdown, combined with weaker bauxite prices and higher freight rates in 2021, was bad for Metro Mining because Bauxite Hills was carrying a lot of project debt. In May and June 2021, the company halted its stock while it worked on a recapitalisation, which raised $25m at 1.6 cents per share and allowed some debt repayments to reschedule. That put Metro in a position not just to handle existing debt, but also work towards a Final Investment Decision on Bauxite Hills Stage 2.

Stage 2 upside

On 16 February 2022, Metro announced that it had completed loading of the final vessels to conclude its 2021 contractual commitments of 3.1 million Wet Metric Tonnes (WMT). Metro's current capacity is 4 million tonnes, but Bauxite Hills Stage 2 would expand that to 6 million. The upside is, potentially, huge. In the March 2017 DFS for Bauxite Hills, which modelled 6 million WMT per annum from year 4 out to the late 2030s, the after-tax NPV was a cool A$601m.

All Stage 2 needs is about A$51m in capex, most of which will be spent on a floating terminal on the Skardon River. Since November 2019, Metro Mining has had a tentative commitment of A$47.5m from the Australian Government's Northern Australia Infrastructure Facility, which means that Stage 2 is more or less funded if the numbers stack up at the time of a Final Investment Decision. And if the NAIF commitment comes good, Metro may be up and running with Stage 2 sometime in the next couple of years.

A Capesize opportunity

Even before Stage 2, Metro Mining's new management has already added value thanks to a floating crane. Up until last year, Bauxite Hills product had to be shipped in Ultramax bulk carriers where the carrying capacity was 60,000- 65,000 DWT. The floating crane meant that Capesize vessels with carrying capacity of 110,000-120,000 DWT could be loaded. The result was a halving of freight rates for Metro Mining when the crane became operational in October.

Then there was Xiangsen Aluminum's commitment in December 2021 to take 1.5 million DMT of Bauxite Hills product in 2022. Half of Xiangsen Aluminum is the Xiangyu Group, a Chinese state-owned commodity trader, and the other half is Shanxi Liulin Senze, a Chinese alumina supplier. The Xiangsen agreement is good for Metro because it indicates that the buyers are likely out there for the extra product that will become available with Stage 2.

A big trend over the next decade in China will be a reduction in use of domestic bauxite by alumina refineries, for environmental reasons, and an increase in imports. That puts Weipa in the box seat for future sales, given how much closer it is to China than two other major producers – Guinea in West Africa, and Brazil – and given Indonesia's stance against the export of bauxite in favour of developing a domestic alumina industry.

With bauxite prices now stabilising, and the potential for a Final Investment Decision regarding Bauxite Hills Stage 2 late this year, Metro Mining stock is now showing signs of life. There's still some risk in this one, in terms of the potential for the stock to crash if Stage 2 doesn't eventuate soon, but for investors comfortable with that risk, Metro Mining is four stars.

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