STOCKS DOWN UNDER

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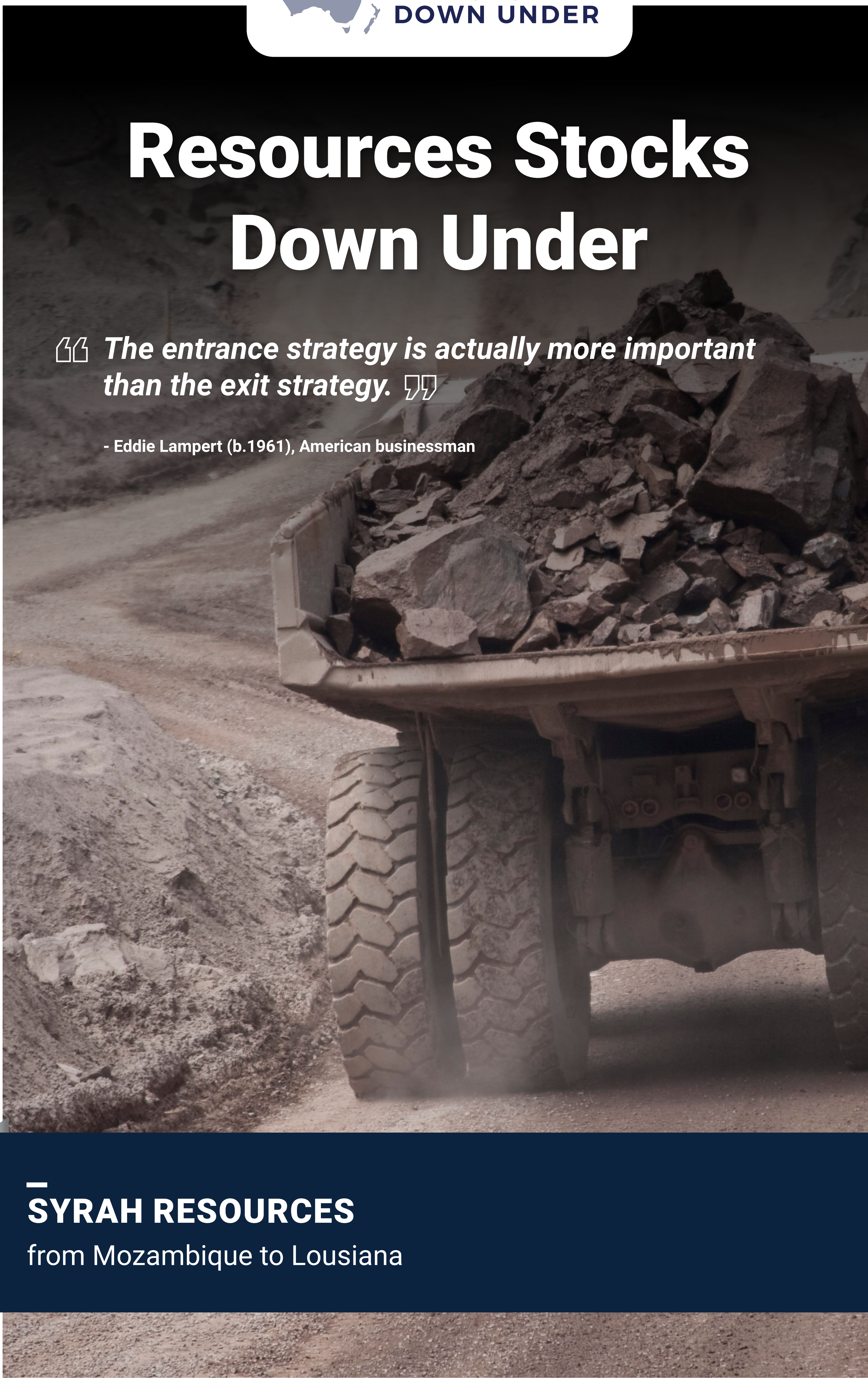
Resources Stocks Down Under



"The entrance strategy is actually more important than the exit strategy."

- Eddie Lampert (b.1961), American businessman

SYRAH RESOURCES

from Mozambique to Lousiana

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Stocks Down Under rating: ★★★★

ASX: SYR
Market cap: A$668.8M

52-week range: A$0.91 / A$2.13
Share price: A$1.33

When we last looked at Syrah Resources in Stocks Down Under in February 2020 the share price was 53.5 cents and we rated it four stars. We took the view that the owner of the Balama Graphite Mine in Mozambique would enjoy better pricing and lower costs in 2020 and beyond. Syrah stock went to 15 cents in the Corona Crash the month after our article, but by November 2020 our original call was starting to come right. We've remained very right since then, helped by a move to further downstream processing in the United States.

Share price chart

Source: Tradingview

In early 2020, when we [first looked at Syrah Resources](), we focused on the original 'company maker', a large graphite mine in Mozambique called Balama, which Syrah had been working on since 2012 and which it brought into production in late 2017. Balama, which lies around 250km west of the northern Mozambican port town of Pemba, is a monster of a graphite mine. Indeed, it's the biggest graphite mine in the world, with a current reserve of 108 million tonnes at 16% TGC (Total Graphitic Content). With an annual processing plant capacity of 2 million tonnes, Balama can operate for more than 50 years pumping out 350,000 tonnes of graphite concentrate every year. And there's more where that came from because the Balama resource is 1,422 million tonnes at 10% TGC.

Moving up the value chain

Alas, 2020 was not Balama's year. Syrah chose to temporarily suspend production in late March 2020 as a result of COVID-19 and production didn't restart until almost a full year later, in March 2021. Most of 2021 wasn't crash hot either, with total output for the year of only 72,000 tonnes of natural graphite, whereas in 2019 it was on track to do 180,000 tonnes before the September 2019 production cuts implemented because of poor pricing at that time. And 180,000 tonnes is only about half of the mine's nameplate.

Which begs the question as to why the share price of Syrah Resources recovered so smartly after the Corona Crash. We think that's got a lot to do with the company's second 'company maker', an Active Anode Material (AAM) plant that Syrah intends to build in the US state of Louisiana. Graphite, you'll recall, is the core ingredient in the anodes of lithium-ion batteries and the best kind of natural graphite to make battery-grade material is the fines that predominate in Balama's output. So, it made sense early on to explore where Balama ore could be upgraded to make AAM, a graphite product suitable to go into such batteries.

Syrah is now a Vidalia story

Syrah was first able to demonstrate in 2014 that it could produce spherical graphite produced from Balama flake and the following year it did its first economic assessment for an American plant making AAM, which is coated spherical graphite. By 2018 Syrah had bought the site of the plant, at Vidalia, a town on the west bank of the Mississippi River about 170 miles north of New Orleans. A qualification plant started producing in 2019 and by December 2020 a Bankable Feasibility Study for a commercial scale plant at Vidalia had published some encouraging numbers.

Syrah didn't publish an NPV for Vidalia in 2020, but it did show that a plant making 10,000 tonnes of AAM per annum could make the product for an All-In Sustaining Cost (AISC) of about US$3,150. At the time the reported selling price for Chinese AAM was about US$5,500. So, it looked like the economics of Vidalia were robust, particularly since the initial 10,000 tpa plant would only cost US$138m to build. And those economics could potentially get better with a 40,000-tonne capacity because then the AISC would come down to about US$2,700.

However, more important than the economics was the fact that before Syrah no one had moved to wrest control of the supply chain for AAM from Chinese suppliers. The market figured that there would be a lot of takers for Vidalia material from US battery makers once that material became available, making it easy to get the project off the drawing back. Which was why the Syrah share price was above the level of our initial call by the end of 2020.

Exquisite timing

Two days before Christmas 2021, Syrah bagged the elephant, announcing that Tesla had signed a binding offtake agreement for the majority of the 10,000-tonne per annum AAM operation and had taken an option over product from the 40,000 tonnes per annum proposal. No surprises, then, that a Final Investment Decision for Vidalia was announced on 7 February 2022. Vidalia will now go to 11,250 tonnes per annum and cost US$176m, but that will be funded by a recently-completed A$250m (US$178m) capital raising. The expanded Vidalia plant is expected to start producing in the September 2023 quarter.

The timing of the Tesla offtake and the Vidalia Final Investment Decision is exquisite. As we've noted a number of times lately in Resources Stocks Down Under, the time is right for graphite plays on ASX because the battery minerals sector is back with a vengeance. We saw lithium plays do well through 2021 on the expectation that the Electric Vehicle sector will continue to expand. Now we think it's graphite's turn.

With Syrah now definitely headed up the value curve, this one remains four stars. Mind you, markets have been choppy lately, so it's probably worthwhile waiting for the rights issue to be completed to see where the share price settles.

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