



Resources Stocks Down Under

📖 *Earn with your mind, not your time.* 📖

- Naval Rivikant (b. 1974), founder of AngelList

EVOLUTION ENERGY MINERALS

Is Chilalo finally all systems go?

EVOLUTION ENERGY MINERALS

Is Chilalo finally all systems go?

Stocks Down Under rating: ★★★★★

ASX: EV1
Market cap: A\$47.3M

52-week range: A\$0.205 / A\$0.565
Share price: A\$0.23

Evolution Energy Minerals (ASX:EV1) is the current owner of the Chilalo Graphite Project in Tanzania. Long-term ASX resources investors would be aware that the Chilalo project has offered promise, but has never gotten off the ground, even though there have been several attempts by multiple companies to make it happen. This failure has mostly been because of the changing regulatory environment in Tanzania, but also an inability to secure finance as a consequence. Is Evolution the company that finally kick starts this project? We think that if Evolution can't do it, no one can.

Share price chart



Source: Tradingview

Chilalo

The Chilalo Graphite deposit is in the Ruangwa District in south-eastern Tanzania, approximately 180km west of the coastal port city of Mtwara on the Indian Ocean and 400km south of Dar es Salaam, the nation's largest city. Drilling campaigns since 2014 have generated an Indicated and Inferred Resource of 67mt at 5.4% Total Graphitic Carbon (TGC). A specific 20mt core contains a grade of 9.9% TGC for around 2mt of contained graphite, making this core one of the higher-grade graphite deposits in its own right.

The Chilalo project was first drawn to investors' attention in 2016 when then owner IMX Resources spun it out into a company called Graphex Mining. After an initial post-listing surge, the company's share price never recovered following the 2017 regulatory changes in Tanzania, which we will address below. Graphex ended up acquiring a gold project in Mali, renaming itself Mali Gold in the process, and spinning out Chilalo into Evolution Energy Minerals.

Enhancing the DFS

The key event for Chilalo since 2016 has been a Definitive Feasibility Study (DFS) released in January 2020. The DFS confirmed the project's potential. Chilalo had a post-tax NPV of US\$331m and post-tax IRR of 36% on a capital cost of US\$87.4m. The payback period was just 3.5 years, while the mine life was 18 years.

Unfortunately for shareholders, Chilalo's capex and opex were higher than outlined in the PFS, which had been issued less than 18 months earlier. It also meant that the project was no longer more appealing than the projects of its closest graphite peers - Black Rock Mining (ASX: BKT) and Walkabout Resources (ASX: WKT).

As a consequence, a proposed US\$85m funding deal with private investment firm Castlelake never went ahead. Recognising the need to enhance the DFS, Evolution has been working on an updated DFS that is expected to be released in the coming weeks. Evolution appointed ex-Syrah Resources project manager Michael Bourguignon to update the DFS. When he was hired, Bourguignon told Evolution shareholders that there were a number of opportunities for cost savings, particularly in relation to mining costs and electrical power.

There have been other positive developments since Evolution's spin-out in November 2021. The most important was a binding offtake agreement with Chinese graphite processor Yichang Xincheng Graphite China (YXGC). The deal covers the sale of 30,000tpa of coarse flake graphite for a minimum of the first three years of production - over 50% of Chilalo's production and 70% of forecast revenue over that time. Another development was the hiring of financial advisory firm Auramet International to advise and secure project funding for Chilalo. Auramet's task at hand will become clearer once the DFS is updated, given we will then know just how much capital is needed.

Watch the Tanzanian government

As we noted above, the Chilalo project has struggled to gain traction since new regulations introduced by then Tanzanian president John Magufuli in 2017. Among the worst of them were the forced renegotiation of existing agreements between resources companies and the government, the restriction of repatriation of funds derived from mining activities, increased royalty rates and a mandatory 16% government shareholding in resources projects.

Magufuli died in 2021 and was succeeded by Samia Suluhu Hassan. It has been a key priority of the new government to improve the business climate, particularly in the resources sector. The government aims to boost the mining sector's contribution to at least 10% of GDP by 2025. We think that investors can be confident in Tanzania as an investment destination, at least for now. We can't blame investors still for being cautious about Tanzania, however, especially because Magufuli's laws were introduced without any prior notice. Evolution has obtained the government's approval of its Resettlement Action Plan (RAP) for the communities living in the vicinity of Chilalo. But it hasn't gone as far as Black Rock Mining, which has signed a formal Framework Agreement with the government. This agreement provides for the government's equity stake and consequential joint venture. It would be more reassuring to us if Evolution Energy Minerals had something similar.

It's now or never

If Evolution cannot get Chilalo off the ground, it is difficult to see any other company ever accomplishing this feat. We observe that the YXGC deal includes a clause stating that the deal is essentially null and void if production at Chilalo cannot start before 31 March 2024. As long as Evolution can complete its DFS in the first couple of months of 2023, we think it can secure financing and enter production before next year's deadline.

For investors comfortable with the regulatory and funding risks – which we acknowledge are higher than many other ASX resources companies in other jurisdictions, including other nations in Africa – we think Evolution Energy Minerals is four stars.



Pitt Street Research Pty Ltd

3 Spring Street, Sydney, NSW 2000, Australia

Stocks Down Under gives you an information advantage to better invest and trade in ASX-listed stocks!

Stocks Down Under (Pitt Street Research AFSL 1265112) provides actionable investment ideas on ASX-listed stocks. The Content is financial advice but is not (and cannot be construed or relied upon as) personal financial advice. No investment objectives, financial circumstances or needs of any individual have been taken into consideration in the preparation of the Content. Please make sure that investing in such products is suitable for your circumstances, and ensure you obtain, read and understand any applicable offer document.

Financial products are complex, entail risk of loss, may rise and fall, and are impacted by a range of unpredictable market and economic factors.

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without prior written permission from Pitt Street Research Ltd Pty. All intellectual property relating to the Content vests with Pitt Street Research/ Stocks Down Under unless otherwise noted.

Stocks Down Under/Pitt Street Research directors and staff may own shares in the companies mentioned in our articles, videos, reports and analyses.

You are receiving this email because you subscribed to our newsletter.

