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China gives Aspire second chance

Aspire Mining offers rare direct leverage to China's 'Belt and Road' (B&R) investment splurge as its once problematic exposure to Mongolia benefits from Beijing's ambitious transport plans.

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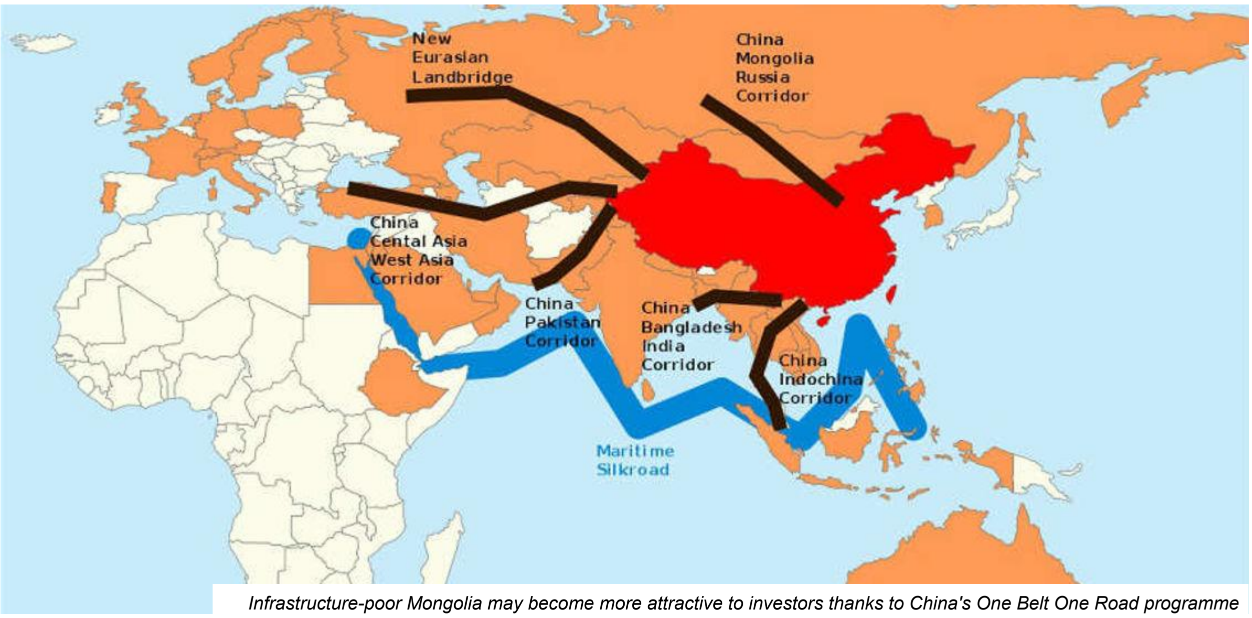

Infrastructure-poor Mongolia may become more attractive to investors thanks to China's One Belt One Road programme

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Speaking in June 2017, BHP's chief commercial officer said China's B&R infrastructure initiative "is expected to trigger huge demand for resources".

A leading international consulting firm has predicted China will mobilise up to US$1 trillion of outbound state financing in the coming decade.

One participant at the International Mining and Resources Conference in Melbourne in November spoke forcefully about the impact on metal markets from an estimated US$70 billion a year being spent on B&R infrastructure.

Seemingly big numbers, taken out of context, can easily exaggerate the importance of the impending windfall for the mining industry.

International Monetary Fund data suggest Chinese investment spending made up 42% of the country's GDP in 2016 or 31.5 trillion yuan (US$4.7 trillion). In other words, US$70 billion would amount to only 1.5% of China's current capital spending and only 0.6% of its GDP, which is expanding 10 times faster.

Over 2002-10, each US$1 billion in China's incremental investment spending came with extra apparent consumption of 190,000 tonnes.

In a global context, US$70 billion a year is not an especially big number. China's experience implies a one-off increase in global steel usage of less than 1% from this level of spending.

China's global investment agenda is partly motivated by an effort to support underused domestic manufacturing capacity which, without B&R, would be slated for closure.

B&R will also allow Chinese financial intermediaries to redirect some of their capital resources away from domestic capacity expansions to more productive outlets elsewhere, lowering systemic risks identified by the national government as well as international agencies.

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Calculating the net gain in global raw material usage needs to take account of already falling growth within a restructuring China.

The greatest economic gains from B&R will come if the Chinese sponsored infrastructure initiatives permit the participation of local businesses in global supply chains or encourage them to kick start production that would not otherwise have been possible.

Those countries that have embraced the Chinese B&R initiative most enthusiastically are also among the most economically vulnerable. Their capacities to take advantage of Chinese investment blandishments vary considerably.

In this realm of diffused economic benefits heavily biased towards the interests of Chinese firms and China's short term national economic goals, few direct mining opportunities exist presently for advanced country portfolio investors.

Aspire Mining is positioned to benefit directly from China's investment efforts.

Aspire came to market as Windy Knob Resources in 2007. At the top of the cycle when coking coal prices were topping US$300/t, the company had a peak market value of A$611 million (US461 million). Today, that is 98% lower.

David Paull, the chief executive of the company, will readily concede he must reboot the company's strategy.

The coking coal assets it had intended to develop in northern Mongolia have been stuck in limbo. Aspire has estimated reserves of 255 million tonnes of high quality coking coal near the largest steel making nation in the world but lacks the necessary infrastructure to get product to market.

Aspire has a concession from the cash-strapped Mongolian government to build a rail line east from the Ovoot coking coal deposit to Erdenet along the planned northern rail corridor running from China to Russia.

A study completed in January this year put the rail capital cost at US$1.25 billion, way too much for a company with a market capitalisation of A$13 million, no cash flows, an unsustainable debt and a large shareholder with its own financial stresses.

In 2014, Aspire added a 45% interest in a smaller coking coal deposit at Nuurstei to its assets. Taking that holding to 90% in August 2017 has given the company a few extra degrees of freedom to help recast the strategy.

Paull has outlined a plan to recapitalise the business, start production at Nuurstei, build his cash flows and use the momentum behind B&R to get his vital rail infrastructure for the main game.

The company completed an underwritten rights issue in early December. The A$16.5 million raising will be enough to pay down most of its US$6.65 million debt to Noble Group and leave it with enough to pursue development of Nuurstei, expected to cost up to US$14 million. With advances against future sales and contractor financing, Aspire expects first production early in 2019.

The logistics are not ideal. From a 12Mt resource, the company will have to truck an anticipated 400-500,000t per annum from a newly constructed wash plant some 430km to a rail loading point at Erdenet from where it will be railed to China and the steel mining centres in Hebei province.

At current prices and despite the transport challenges, Aspire should be able to achieve similar margins on its sales as those producers in Australia and North America with which it will have to compete for steel mill access near the Chinese coast.

For the main game, Aspire must rely on China Gezhouba Group. The Chinese company will get a 51% interest in the northern rail concession if it can persuade Chinese officials to back the link as part of the grander plan to run a rail line through central Mongolia to Russia.

The 2017 Mining Journal World Risk Report (feat.MineHutte ratings) gave Mongolia a highly cautionary CCC rating. None of the 85 jurisdictions reviewed received a lower infrastructure score.

For some, the Mining Journal rating might be good enough reason to stay away. Paull believes the government, now working within an IMF bailout agreement, is unlikely to repeat the mistakes reflected in the Mining Journal lowly risk rating.

Paull now needs a favourable decision from Beijing bureaucrats and his state-owned Chinese business partner to tip the development balance - likely but no foregone conclusion.

Many investors will have understandably lost patience but the company appears to have conjured a second chance through an unusually direct leverage to the B&R roll-out.

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