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Kasbah’s doubtful destiny

Amazingly, Kasbah Resources was the top performing ASX-listed mining stock in March and one of the top three in the first quarter of 2020.

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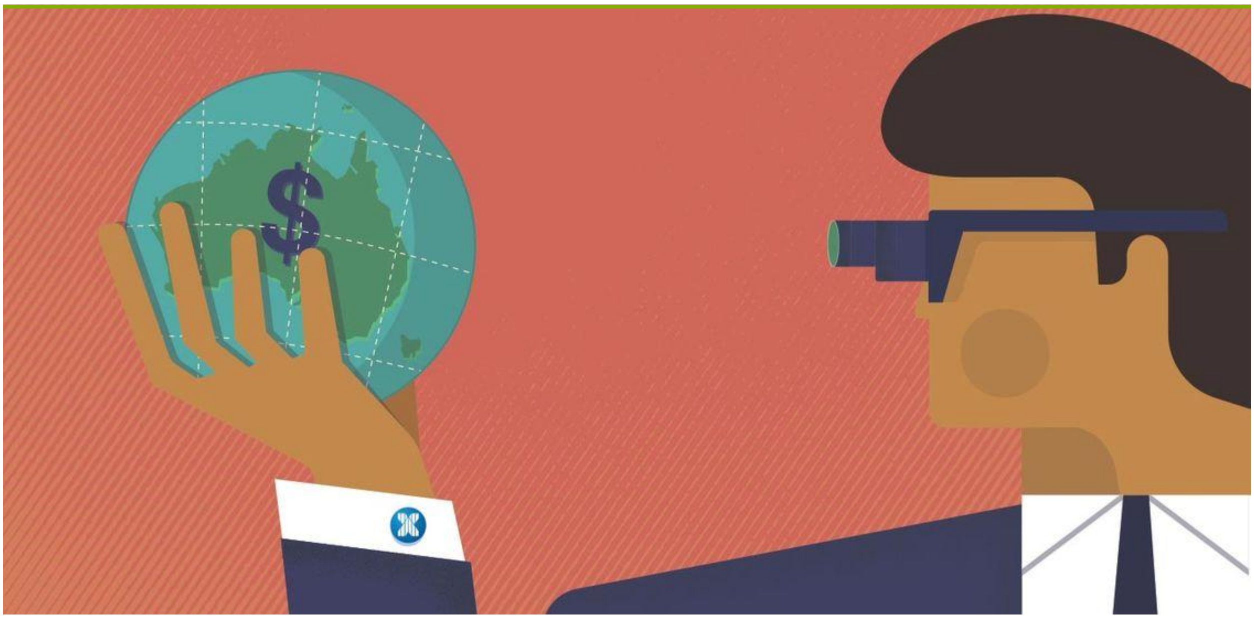

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The Moroccan tin mine developer posted a 322% share-price rise over the last seven trading days of March. A 245% gain over the entire month compared with a 25% median decline in the price of sector stocks battered by the COVID-19 pandemic.

The company itself had made no formal disclosure that might explain such a steep ascent in its market value. The last public comment from directors could easily have been grounds for the share price to shed even more than its 93% loss since January 2019.

On March 9, the Kasbah board advised that the macro conditions arising from the COVID-19 pandemic "will have an impact on the ability for Kasbah to successfully secure project funding, strategic partnerships or find corporate opportunities for the business in the short-to-medium term". Directors warned of insufficient funds to navigate the challenging conditions over the next 12-18 months.

In theory, any end of March share buyers would have been eyeing a handsome profit. In practice, they only risked A$6,261 (US$3,900) plus brokerage in an otherwise illiquid and disengaged market. Now, with a 170% spread between the March closing price and the highest market bid, any profits could just as quickly unravel.

Kasbah is a microcosm of the agonising plight of so many miners marooned in the commercial no man's land between resource definition and mine construction.

The Achmmach tin project was once slated for a development decision in 2009. Based on the original game plan, the mine should be close to exhaustion and not further away from a construction commitment than ever.

Backed by some big names in the tin industry, a succession of directors has repeatedly portrayed the company as being on the cusp of landmark funding deals.

As my August 9, 2018 column pointed out, the mine's positive but ultimately modest financial attributes have left the company trapped with a mineral resource not quite good enough to command the needed capital.

“ **Companies will need to put aside wishful thinking in favour of a considered assessment of alternative scenarios**

Instead, memories of past disappointments and unrewarded expenditure of A$80 million weigh heavily. Betraying unjustifiably inflated expectations, directors characterised the reticence of shareholders to contribute more as "underwhelming" after capital raising efforts last year hit a wall.

Remaining retail investors risk heavy equity dilution. Borrowings of A$6.9 million accruing interest at 15% and A$160 million in development capital needs could easily swamp the A$3.4 million market capitalisation and A$912,000 in cash assets.

The company's potential earnings and value proposition are highly leveraged to the tin price. When the company launched in 2007, the tin price was sitting around US$15,000 per tonne and on the rise. Subsequently higher prices could not hold.

By mid 2009 and again in mid 2015, at critical junctures in the decision-making processes, the price reverted to its 2007 levels, as it has done once again. Today's tin price is not sufficient for mine development to proceed. But it keeps recurring.

For any miner, the low metal price in a well-established trading range must be survivable. Proceeding on the assumption it will never happen again invites disaster.

The optimistic judgements presented to ordinary shareholders over the years could best be described as wishful thinking rather than the product of rigorous analysis. Directors have been prone to quote conveniently bullish investment bank forecasters with little regard to their track records. Nor have those with contrary opinions been recognised.

As recently as January, even as the tin price had been declining for nearly a year, directors were of the view that "the long-term market fundamentals remain unchanged and prices are expected to rise over the medium term".

The COVID-19 pandemic looks to have radically altered the economic landscape, although the full extent of the change remains hard to assess. All companies will have to be flexible enough to adapt their thinking to a wide range of alternative scenarios. That said, a scenario in which metal demand is much higher than previously thought likely appears only a dimly remote possibility.

Rates of economic activity, even in the event of a swift reopening of currently shuttered businesses, could come with greatly reduced metal needs. At the same time, investors are showing signs of becoming more sensitive to corporate risk profiles. Miners will have to reconsider project valuations if funding is priced and rationed accordingly.

Meanwhile, those retail investors who had once backed Kasbah Resources, and hundreds of like companies, will have had the value of their investible funds slashed, whether they had held mining investments or supposedly safer equity exposures. Their propensity to support the sector has fallen, intensifying the struggle for capital.

To regain credibility, companies will need to put aside wishful thinking in favour of a considered assessment of alternative scenarios with a view to moving appropriately once the evidence begins to form around one of the possibilities.

Prematurely picking one scenario over another is an analytical lucky dip. Cutting and pasting old commentaries to attract investors is simply misleading. Perhaps, in this climate, even ‘walk away' needs to become a strategic option.

In a bleaker economic landscape, gravely undercapitalised companies like Kasbah will also further test the patience of governments more desperate than ever for new revenue and employment sources.

One day, Achmmach will be a mine. How long that takes, whether the buyers in late March benefit or whether Kasbah has any involvement, will depend on how low the new starting point for economic activity is eventually depressed.

Kasbah shareholders must now contemplate a sobering range of alternatives. The possibility of a 2021 development start permitted by a quick economic turnaround, or a mid-decade restoration of metal demand as the global economy slowly recovers, or another 13 years of plans disrupted by volatile markets - this range implies vastly different decisions today about the best way forward.

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