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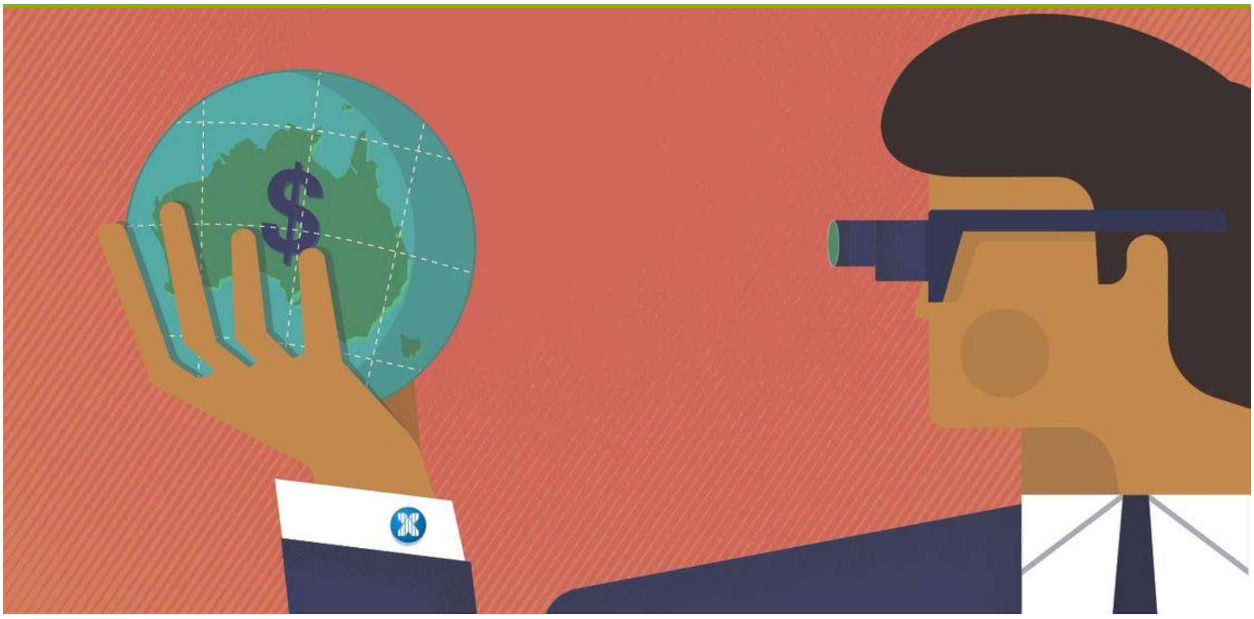
Fourth time lucky for Kasbah

Kasbah Resources is running out of options as it releases its fourth definitive feasibility study since 2014 for its 75%-owned Achmmach tin deposit in Morocco.

John Robertson*



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A new feasibility study has posited a 10-year mine life, starting in late 2020, during which time the project joint venturers expect to recover some 44,390 tonnes of tin in concentrate at a cost of US$9,176 per tonne of metal content. Pre-development capital of US$96.4 million and sustaining capital of US$69.2 million would be needed for a post-tax value of US$98.1 million, according to Kasbah directors.

Speaking in Melbourne to an audience of several hundred a day or two after releasing a summary of the study on July 16, chief executive Russell Clark characterised the tenfold disparity between the company's lowly A$12 million (US$8.9 million) market capitalisation and the project value as indicative of the share-price upside investors could expect.

This latest study of the project economics is the fourth described as "definitive" as the company has juggled key parameters to define a path capable of attracting investment funding.

In March 2014, the company was contemplating a much larger capital commitment. It planned to spend US$181 million ahead of producing 45,900t of tin for a project valuation of US$126 million. A US$23,025/t tin price could produce life-of-mine post-tax cash flows of US$270 million, it said. This would have been equivalent to a 7.6% annual bond yield for a portfolio equity investment at the time.

The second variant published in March 2015 described a reduced US$148 million investment. Life-of-mine tin production was raised to 51,200t at a slightly lower cash cost. The company put a value on the revised project of US$171 million using a US$21,511/t tin price to push the implied return for equity investors to slightly over 10%.

In July 2016, with capital sourcing for the industry proving problematic, the company came up with a scaled back version. It would spend only US$61.7 million, cut production to 41,680t and reduce the mine life by a year. If the tin price had not changed for the worse, this variant would have pushed the return higher.

> **The company now has only two options, assuming giving up is not one**

At the US$17,830/t price assumed for study purposes, on the other hand, a US$72 million outlay for equity and development capital was set to generate less than US$95 million over the 13 years of planning, construction and production for an unimpressively low single-digit return.

The effect of tin price movements on the corporate return analysis has overwhelmed contemplated operational or strategic changes.

Applying the same tin price assumption across the four studies points to the 2014 variant being the least compelling, unsurprisingly given the capital outlay. While the differences between the last three analyses are not large. The latest study offers the least compelling economic case for development.

The latest plans, at the current sub-US$20,000 tin price, imply a bond yield equivalent for an investment in Kasbah Resources of around 6%. The company is not cheap.

Kasbah directors have sought to break the nexus between historical prices and development decisions by framing the contemporary decision as a response to a future of potential tin market deficits leading to higher prices.

The Kasbah feasibility study itself hints at the problem with this approach when it correctly concedes "ongoing market deficits will not be sustainable going forward". The world cannot use more metal than exists. Some combination of new production, substitution effects and more efficient metal use will restore balance.

Forecasting price outcomes over the duration of a project is more complex than simply asserting that they will be permanently higher while ignoring second and third-round feedback loops involving producers and users of metal responding to price incentives. Investors know this, even if only intuitively. No wonder they tend to place little credence on more simplistic analyses.

A lengthier mine life would have been a surer route to an improved valuation for the company. That would have required a larger defined mineral resource and, inevitably, more spending on drilling and analysis and, with that, more equity.

The company has already spent around US$70 million which, if included, would dramatically shrink any return calculations.

Company executives have always expressed optimism about the ultimate size of the Achmmach project but the disjointed nature of the mineralisation within the immediate region has mitigated against consolidating a larger resource. Efforts to conserve expensive capital have come at a cost.

Two years on, the company appears less advanced than it was when it had supposedly lined up finance, offtake and development plans in 2016 only to forgo the opportunity in expectation of better deals when tin prices had risen.

The company now has only two options, assuming giving up is not one. Build a bigger resource to improve the economics or take whatever funding deal is on offer in the hope tin prices paper over earlier misjudgements.

As for share price performance, Clark has fallen into the trap of using a valuation based on an unsubstantiated discount rate to lure investors, although he is hardly alone in that bad industry habit. His predecessor as chief executive also used 8% even as higher-risk corporate bond yields were topping out at a record 20%. Mysteriously, the company's assumed cost of capital has borne no relationship to financial market conditions, a possible explanation for why seemingly attractive valuations never translated into development success.

Today, some miners are effectively paying 14% for development funding after taking account of interest, fees, royalties and gifted equity. Kasbah would be diverting value from its ordinary shareholders if that was its marginal cost of finance.

Without evidence to support more attractive funding costs, the case for repricing the company's equity is weak.

The long-touted enthusiasm of the company's joint venture partners to help with funding will now be tested. Tin prices aside, cheap Japanese money might be the single biggest contributor to getting development underway and improved equity values.

**John Robertson is the chief investment strategist for PortfolioDirect, an Australia-based equity research and resource stock rating group. He has worked as a policy economist, business strategist and investment professional for nearly 30 years, after starting his career as a federal treasury economist in Canberra, Australia*