

# Sirius priced for bright future

The company's early success is a tough act to follow



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**S**irius Resources NL is speeding its way to a mine development in the Fraser Range region of Western Australia. In a cycle characterised by delays, false starts and dashed expectations, Sirius is setting new standards for exploration insight, development opportunity and investment returns. The question for investors is how to approach a company already priced for success.

On July 16, Sirius' managing director Mark Bennett offered another round of exciting exploration results from a Fraser Range drilling programme. He expressed his surprise at the quality of the outcome at the first hole drilled at the company's Taipan prospect.

The market reaction this time was far less exuberant than the reaction in 2012, when the company announced it had discovered "an entirely new unexplored nickel province". Within a week, the price had risen tenfold and would soar 8,200% inside a year.

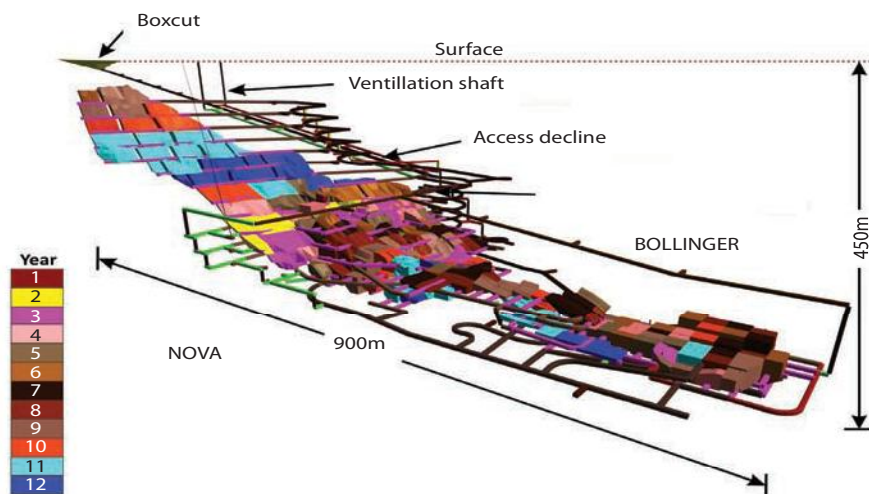
This month, the share price added just 15% for the day and actually dropped 3% a day later. Now, with a market value sitting around A\$1.4 billion (US\$1.3 billion), after taking account of escrowed stock and unexpired options, getting meaningful market responses to exploration outcomes is tougher.

On July 14, Sirius released the details of a definitive feasibility study for the development of the Nova-Bollinger deposits that arose from the 2012 discovery. The study was framed around a mine life of 10 years to produce 26,000t of nickel, 11,500/t of copper and 850/t of cobalt a year. The plan to mine 1.5Mt/y of ore would cost A\$125/t or an all-in sustaining cash cost of US\$3.47/lb of nickel before by-product credits of US\$1.38/t.

The company is aiming for a commitment to mine by the end of 2014 with first sales early in 2017. This will be a tall order, but the cycle is probably on the company's side. Delays due to skill shortages, equipment lead times and overworked consultants are less likely.

Sirius is making the transition from explorer to miner and, as it does, the way it is viewed by investors will change. This is usually a time of rising risk for investors as potential delays, cost escalations and revisions to project economics frequently bias the share price to the downside. Progressively, greater attention is paid to the underlying value proposition and less to discovery events.

During a transition, the market displays a



**A new mine at Nova-Bollinger is expected to produce 26,000t/y of nickel, 11,500t/y of copper and 850t/y of cobalt for at least 10 years**

tendency to reprice equities based on more clearly defined project economics to get a return that adequately compensates for the risks and the time value of money for an equity investor. Kasbah Resources is a good recent example of this market phenomenon. Its share price has fallen by one-third since it released its definitive feasibility study for the Moroccan Achmmach tin project at the end of March.

In contrast to the more typical company experience, Sirius Resources has been the most strongly performing stock among the 1,000 or so making up the Australian-listed resources sector over the past 12 months and one of the five best performing over the course of the current market cycle. So far, there has been little hint of the malaise afflicting the likes of Kasbah Resources.

The market's treatment of Sirius is a tribute to the people running the company. An investor must now make a judgement about whether they can do enough to sustain this quality premium. The pressure is on.

The A\$1.4 billion market value of the company, a A\$473 million pre-production capital requirement and the prospective cash flow of A\$2.74 billion over 10 years from Nova-Bollinger described in the definitive feasibility study imply an annual return over 12.5 years from an investment today of just 4.3%.

A return barely superior to government bond yields is inadequate compensation for the risk incurred through equity investment. A more appropriate return and one more commensurate with what is available elsewhere in the market would require the Sirius share price to be significantly lower than the A\$3.90/share level at which it is trading. An 8% return, put-

ting it line with the Kasbah valuation, would require a share price around A\$2.20/share.

The apparently low return on current plans could be averted if the company materially extends the anticipated mine life or increases the production rate. Neither of these possibilities is out of the question as the announcement about Taipan intimates. The company's impressive track record will be taken by some as enough evidence that both enhancements are foregone conclusions.

For that to be so, the recently released study would not have been definitive but just another analytical input along the path to a bigger project. This is where things get difficult. Changing plans risks delays. While a longer life or higher throughput project could be the financially rational course, shuffling timelines may disappoint investors. Some may start to think Sirius is not so different after all. The company is now hostage to its success.

No doubt this choice will be playing on the minds of Sirius directors as they contemplate their options. So far, they appear to have made a judgement that the speediest possible development commitment is the best way forward with adjustments to the operating scale to come at a later time.

The company has said that projected financial returns are highly sensitive to assumptions about the nickel price, but that changes the reason for investing. To the extent commodity prices are correlated, and higher nickel prices are part of a broad-based cyclical improvement in conditions, there will be companies more leveraged to such changes than Sirius Resources as it makes its transition from high flying explorer to a more dour market leader. ▼