EDISON

Almonty Industries

Valuation update

Woulfe transaction implications

Metals & mining

Following the recent transaction to acquire Woulfe Mining's equity and debt, Almonty has proposed a merger of the companies, which would give Woulfe shareholders c 40% share in the combined entity. Woulfe's main asset is the past-producing Sangdong tungsten project, which boasts low opex, capital intensity and a relatively short lead time. We have attempted a preliminary valuation of the project, estimating its NPV_{10} at C$0.7 per Almonty share on a funded and fully diluted basis, using a US$300/mtu APT price and assuming the IMC JV goes ahead.

Year end	Revenue (C$m)	PBT* (C$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
09/13	18.3	0.6	1.6	0.0	50.0	N/A
09/14	29.6	9.9	25.4	2.6	3.1	3.3
09/15e	35.3	(6.9)	(13.7)	0.0	N/A	N/A

Note: *PBT and EPS are normalised, excluding intangible amortisation, exceptional items and share-based payments. Financials unchanged until more details are released.

Sangdong: Low opex and capex intensity project

On 7 July Almonty announced that it had entered into an agreement to acquire Woulfe Mining, valuing the company at c C$26m. Woulfe's flagship asset is the past-producing Sangdong tungsten project in South Korea. It is one of the few advanced, large-scale tungsten projects to have been brought through technical studies and permitted, but is yet to secure funding. Due to its brownfield nature and high-grade mineral resource, the project is expected to have low opex and capex intensity. Apart from the robust project economics, Woulfe's strong advantage is a JV agreement with IMC, one of the largest consumers of tungsten, which we understand is still supportive of the project.

Tungsten market conditions remain difficult

Tungsten has not been immune to the overall deterioration in the commodity space, with the benchmark APT price recently sliding to US$215/mtu, a 34% reduction ytd. This price weakness is a result of the slowing Chinese economy and tungsten's high exposure to the mining and oil & gas industries, which have been hit by falling commodity prices. In addition to demand-related concerns, the anticipated increase in new mine supply from Nui Phao in Vietnam and Hemerdon in the UK could keep tungsten prices under pressure.

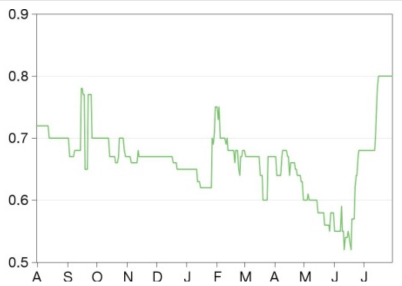
Valuation: IMC engagement is key

We have undertaken a preliminary valuation of the Sangdong project based on operational assumptions from the feasibility study. On an unrisked and unfinanced basis, using a 10% discount rate, an APT price of US$300/mtu and a 20% discount for concentrate, we estimate the project's NPV at US$127m. At the spot APT price of US$215/mtu, the project's value falls to C$23m. On a funded and fully diluted basis, we value the project at C$0.7/Almonty share, assuming IMC acquires a 25% interest in the project, and C$0.9/share if Almonty fully funds the project through equity and debt. Overall, we believe that IMC involvement in the project is crucial as it could provide an offtake and facilitate project finance.

31 July 2015

Price	**C$0.8**
Market cap	**C$42m**
	US$/C$1.25
Net debt (C$m) as at Mar 2015	20.2
Shares in issue	51.9m
Free float	28%
Code	AII
Primary exchange	TSX-V
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	17.7	33.3	11.1
Rel (local)	19.0	41.1	19.9
52-week high/low		C$0.8	C$0.5

Business description

Almonty Industries is an independent tungsten producer, with two operating mines – Los Santos in Spain and Wolfram Camp in Australia – and the development-stage Valtreixal tungsten-tin project in Spain. The company produced 90kmtu of contained WO_3 in FY14 and we expect it to deliver 133kmtu in FY15 as it fully consolidates WCM.

Next event

Q315 financials	August 2015

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Woulfe acquisition: Implications for Almonty

Transaction background and rationale

On 7 July, Almonty announced that it had entered into an agreement to acquire Woulfe Mining by way of a court-approved plan of arrangement. According to the offer, each Woulfe share will be exchanged for 0.1029 shares in Almonty, valuing Woulfe at about C$26m, or C$0.07/share, based on the pre-announcement share price. On completing the transaction, which is expected in early September 2015, Woulfe shareholders will control c 40% of the combined company. The merger follows the earlier announced transaction to acquire 29.5m shares, representing 8% of outstanding capital, and C$5.0m of convertible debentures of Woulfe. The transaction will have to be approved by Woulfe shareholders at an EGM, which is expected to be held on or before 8 September, with a favourable vote of at least 66% required.

Woulfe's flagship asset is the past-producing Sangdong tungsten project in South Korea. It is one of the few advanced and relatively large-scale tungsten projects that have been brought through technical studies and permitted, but yet to secure a funding package. Apart from the robust economics of the Sangdong project, Woulfe's strong advantage is a JV agreement with IMC, one of the largest consumers of tungsten, which we understand is still supportive of the project. IMC could provide an offtake and co-fund the project. Once in production, the Sangdong project could more than triple Almonty's current tungsten production (to c 400-450kmtu of WO_3), potentially leading to the creation of one of the largest independent upstream tungsten producers.

Sangdong: High-grade, low opex and capex intensity project

Sangdong is a past-producing underground tungsten-molybdenum project in South Korea. The recently released feasibility study on the project, which is based on the work completed in 2012, incorporated additional definition drilling, a detailed higher-grade mining model as well as a smaller processing plant to treat higher-grade ore. The project's resource is estimated at 44.0Mt grading 0.42% WO_3 in the indicated and inferred categories, while the reserves estimate stands at 5.9Mt at 0.57% WO_3. We note that the mineral resource was only reported above the minus third level, with the additional (approximately 15) levels below currently flooded. Some of these additional mining levels could potentially be investigated further to increase the resource base and extend the mine life; however, the company has no immediate plans to do this.

Exhibit 1: Sangdong mineral resources

Category	Zone	Tonnage, kt	WO3, %	MoS2, %
Indicated	F2	2,140	0.62	0.04
Indicated	F3	2,040	0.62	0.04
Indicated	Main	5,120	0.46	0.05
Total indicated		**9,300**	**0.53**	**0.04**
Inferred	F2	900	0.45	0.04
Inferred	F3	800	0.45	0.03
Inferred	Halo	8,300	0.28	0.04
Inferred	Hangingwall	24,700	0.42	0.05
Total inferred		**34,700**	**0.39**	**0.05**
Total resources		**44,000**	**0.42**	**0.05**

Source: Woulfe Mining

According to the feasibility study, the project is expected to process 640kt of ore per year at a head grade of 0.57% WO_3, on average producing some 288kmtu of WO_3 per year over the initial mine life of 10 years. The metallurgical recovery is estimated at 81% using a conventional scheelite flotation circuit. Despite the significant molybdenum mineralisation and the fact that the mine produced molybdenum concentrates in the past, we understand that it has been excluded from the project's scope. The project's overall pre-production tungsten-related capex was estimated at US$62.7m, including contingency but excluding import duties and taxes (will be refunded due to using locallysourced equipment). In addition, the project is expected to incur US$19.5m in sustaining capital expenditure over the mine life. The pre-production capex estimate implies an attractive capital intensity of US$218/mtu based on the steady-state annual production of 288kmtu of WO_3. At the same time, the feasibility study estimates the project's direct production cost at US$49.6/tonne, including mining, processing, environmental and direct G&A expenses, which implies an average cost of US$112/mtu of saleable product (ranging from US$90/mtu to US$129/mtu over 10 years). The low opex is driven by the high-grade resource and a relatively high recovery in concentrate. We also note the favourable tax regime in South Korea, with no mining-related royalties and a 24.2% income tax rate. Finally, we note that the project has a relatively short lead time, with an estimated construction period of 20 months. The project has been essentially permitted, with the remaining approvals largely construction-related.

Exhibit 2: Sangdong capex estimate breakdown, US$m

Mine development and equipment	14.7
Processing plant (including contingency)	23.7
Surface infrastructure and mobile equipment	13.2
Owner's costs	11.1
Total pre-production capex	**62.7**
Sustaining capital over LoM	19.5
Total LoM capital expenditure	**82.2**

Source: Woulfe Mining

Exhibit 3: Sangdong direct opex breakdown, US$/tonne

Mining	33.8
Processing and tailings management	11.0
Surface department and G&A	4.9
Total opex, US$/tonne	**49.6**
Total opex, US$/mtu	112

Source: Woulfe Mining

Valuation, financials and financing

Unfinanced valuation of Sangdong

We have undertaken a preliminary valuation of the Sangdong project based on operational assumptions derived from the feasibility study. On an unrisked and unfinanced basis, using a 10% discount rate, a flat APT price of US$300/mtu over LoM and a 20% discount for concentrate, the project's NPV would equate to US$127m (assuming 100% project ownership). At the spot APT price of US$215/mtu, the project's value falls to C$23m. Our valuation does not take into account the likely price discounts to IMC, should both companies continue with the JV.

Exhibit 4: Sangdong's unfinanced NPV (C$m) sensitivity to changes in the APT price and discount rate

		Benchmark APT price, US$/mtu								
		200.0	**225.0**	**250.0**	**275.0**	**300.0**	**325.0**	**350.0**	**375.0**	**400.0**
Discount rate, %	**0.0**	54.0	107.5	160.9	214.4	267.8	321.3	374.8	428.2	481.7
	5.0	24.0	64.0	103.9	143.8	183.8	223.7	263.7	303.6	343.5
	10.0	4.1	34.8	65.6	96.3	$\boxed{127.1}$	157.8	188.5	219.3	250.0
	15.0	-9.4	14.9	39.1	63.4	87.7	111.9	136.2	160.5	184.8
	20.0	-18.8	0.8	20.4	40.0	59.6	79.2	98.8	118.4	138.0

Source: Edison Investment Research

Exhibit 5: Sangdong economics at different APT prices (US$m)

APT price, US$/mtu	200.0	225.0	250.0	275.0	300.0	325.0	350.0	375.0	400.0
Revenue	46.0	51.7	57.5	63.3	69.0	74.8	80.5	86.3	92.0
Cash cost	31.8	31.8	31.8	31.8	31.8	31.8	31.8	31.8	31.8
EBITDA	14.2	19.9	25.7	31.5	37.2	43.0	48.7	54.5	60.2
EBITDA/mtu	**48.1**	**68.1**	**88.1**	**108.1**	**128.1**	**148.1**	**168.1**	**188.1**	**208.1**
DD&A	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9	8.9
EBIT	5.3	11.0	16.8	22.6	28.3	34.1	39.8	45.6	51.3
Tax	1.3	2.7	4.1	5.5	6.8	8.3	9.6	11.0	12.4
NOPAT	4.0	8.3	12.7	17.1	21.5	25.8	30.2	34.6	38.9

Source: Edison Investment Research

Financed valuation of the project and combined company

To estimate the financed valuation of the project we have considered two scenarios:

1. In line with the original agreement, IMC acquires a 25% interest in the project for C$35m (we have assumed C$25m as IMC has already provided C$10m in debt), which will be spent on the project's development, while Almonty funds the remaining portion of capex through equity and debt. Under this scenario, we estimate the project's financed value at C$0.74 per Almonty share on a fully diluted basis (we assume that Almonty completes the acquisition of Woulfe, which would bring the total amount of its shares to 87m, and issues additional 29m shares at the current price of C$0.8 to co-fund the development of Sangdong). Further, adjusting our current valuation of Almonty (C$1.0/share) for the acquisition of Woulfe (35m in new shares plus C$11m in debt from IMC), the combined value of the company and Sangdong project would come in at C$1.2/share on a fully diluted basis.
2. IMC provides an offtake, while Almonty fully funds the development of the Sangdong project through a combination of equity and debt (we have assumed 50/50% split to fund US$71m in pre-production and year one sustaining capex). Under this scenario, we estimate the project's financed and fully diluted value at C$0.88 per Almonty share and the combined valuation at C$1.34/share. We note that our valuation is lower under the first scenario as we assume that IMC acquires 25% in the project below our fair value estimate. While this suggests that the JV agreement is not very favourable for Woulfe, in the prevailing depressed tungsten market conditions the project might be difficult to execute without IMC involvement.

Both valuation scenarios are based on the APT price of US$300/mtu (implied concentrate price of US$240/mtu). At a more conservative APT price of US$250/mtu (concentrate price of US$200/mtu), Sangdong's financed valuation would fall to C$0.38 per Almonty share and C$0.45/share under the two scenarios, respectively. The combined valuation would be C$0.84/share and C$0.91/share respectively.

Impact on Almonty's financials

From a financial perspective, if the company completes the acquisition of Woulfe, we expect minimal implications for Almonty's earnings but a more pronounced impact on the balance sheet. In the nine months to March 2015, Woulfe reported SG&A of C$1.0m, which was primarily made up of staff costs, including management fees, and share-based payments, and are likely to be significantly reduced by Almonty. On the balance sheet side, the company will have to take on its books a C$11m loan from IMC, which matures in September 2015. The future of this loan is likely to be linked to discussions around the final JV agreement between the companies. Overall, we believe that IMC's involvement in the project is key to its success as IMC, being one of the largest downstream consumers of tungsten, could provide an offtake and facilitate project finance, therefore significantly reducing execution risks. That being said, the company believes that its longstanding industry presence and strong customer relationships will enable it to secure an offtake for the project.

At this stage, we are not making any changes to our financial forecasts and valuation. We will update our estimates following the release of Q315 results in August.

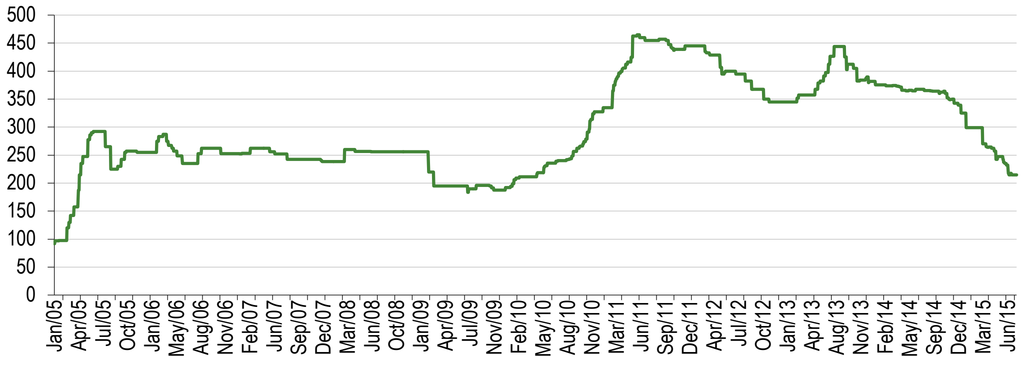
Industry and sector commentary

Tungsten prices remain under pressure

Tungsten is not immune to the overall deterioration in the commodity space, with the benchmark APT price recently sliding to US$215/mtu, a 34% reduction ytd. This price weakness was a result of the slowing Chinese economy as well as tungsten's high exposure to the mining and oil & gas industries, which were hit by falling commodity prices leading to significant capex cutbacks (see Exhibits 7 and 8). In China, the preliminary manufacturing PMI reading in July was 48.2 – the lowest level in 15 months and significantly below the consensus estimate of 49.7. This compares to the June reading of 49.4. On a positive note, however, we highlight a notable improvement in Sandvik's total orders in Q215, which showed a 4% y-o-y contraction compared to an 11% drop in Q115, with mining and machinery orders falling 1% and 4% respectively compared to 11% and 2% reduction in Q115.

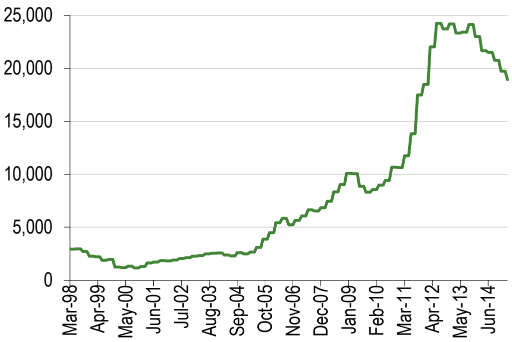
In addition to demand-related concerns, we note the anticipated increase in new mine supply coming from the Nui Phao project in Vietnam and Wolf's Hemerdon mine in the UK. While project-related information has not been publicly disclosed, from our discussions with HC Starck, one of the Nui Phao JV partners, we understand that the project is being gradually ramped-up and is expected to reach full capacity of 6,200t per year (though no details on the timing were provided). At the same time, Wolf Minerals announced wet commissioning of Hemerdon in June 2015. If there is a protracted recovery in demand, new supply could keep tungsten prices under considerable pressure. On the flip side, we would expect higher cost production capacity, such as North American Tungsten's Cantung project (275kmtu of WO_3 production in 2014), to exit the market, potentially easing the oversupply risks.

Exhibit 6: APT price, US$/mtu, FOB Hong Kong



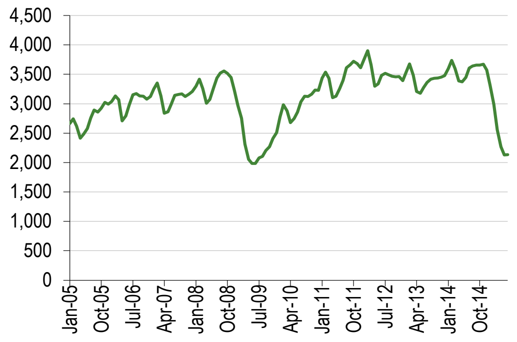
Source: Bloomberg

Exhibit 7: Australia's mining capex, A$m



Source: Bloomberg

Exhibit 8: Global rig count (number of rigs)



Source: Baker Hughes

Tungsten sector news roundup

Below we provide a brief update on the development of the most advanced tungsten projects, which could affect the supply-demand balance over the short to medium term.

On 24 June **Wolf Minerals** announced wet commissioning of the Hemerdon project, which is expected to start commercial production later this year and achieve full production capacity in FY16. We estimate the first full-year production at around 400kmtu of WO_3 as the project will process higher-grade material. On the cost side, our updated model suggests an all-in cash cost of c US$165/mtu in FY16. This includes direct production costs, after tin credits, of c US$111/mtu (including royalties) and debt service costs of c US$50/mtu (average cost of US$42/mtu over LoM). Based on the spot APT price of US$215/mtu and assuming a 20% discount for concentrate, the project could still be cash-flow positive, albeit at a very slim margin. However, the situation may change if tungsten prices stay at the current levels for longer, as we expect Hemerdon's cash cost to increase slightly in FY17 on the back of the lower tungsten grade.

W Resources released a scoping study on the La Parrilla tungsten mine, considering production of 85kmtu pa of WO_3 from mid-2016 before developing the full-scale project to deliver c 340kmtu per year. The initial capex was estimated at just US$16m, with an additional US$36m required to upgrade the project. The unit cash cost after tin credits was reported at US$121/mtu. However, no further details on the cost side were provided. The company has also received an environmental approval for the project. It is, however, yet to sign an offtake and secure funding, both of which may not be easy to achieve given the prevailing difficult market conditions.

Ormonde Mining has closed the Oaktree financing transaction, which is expected to fully-fund the development of the Barruecopardo project in Spain. However, it is not clear if the JV partners are planning to proceed with the project in the current market conditions or if the final investment decision on the project was made. Based on our estimates, at the spot APT price, the project could still be marginally cash-flow positive (EBITDA less tax and interest on debt), but is NPV negative.

Northcliff Resources has recently raised C$2.6m in private placement. The company expects to receive the EIA approval by the end of the year. While this could be an important catalyst for the stock, the company will be looking to raise more funds to advance the project to the final investment decision. Given Northcliff's depressed share price and the recent buy-out of Rutila Resources, we would not rule out Todd, which owns 20.0% in Northcliff and 11.5% directly in Sisson, eventually making an offer for the company. Given the almost 100% premium paid for Rutila shares, this could be an attractive exit opportunity for some of the minority shareholders.

Having secured some short-term funding and filed for court protection under the CCAA, **North American Tungsten** has initiated the asset sale process. Given the high cost and the short remaining mining life of the currently-producing Cantung mine, it is unlikely that the project will stay in business against the current market backdrop.

Exhibit 9: Financial summary

C$000s	2013	2014	2015e	2016e
Year-end September	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS				
Revenue	18,341	29,609	35,282	42,197
Cash cost of Sales	11,400	10,287	28,309	23,320
Gross Profit	6,941	19,322	6,973	18,877
EBITDA	4,138	16,109	939	13,442
Operating Profit (before except.)	691	11,499	(5,232)	7,429
Exceptional items	0	0	0	0
Other	0	0	0	0
Operating Profit	691	11,499	(5,232)	7,429
Net Interest	214	443	1,086	2,210
Profit Before Tax (norm)	602	9,893	(6,918)	4,619
Profit Before Tax (FRS 3)	602	9,893	(6,918)	4,619
Tax	0	0	0	0
Profit After Tax (norm)	602	9,893	(6,918)	4,619
Profit After Tax (FRS 3)	602	9,893	(6,918)	4,619
Average Number of Shares Outstanding (m)	37.0	38.9	50.4	51.9
EPS - normalised (c)	1.6	25.4	(13.7)	8.9
EPS - normalised and fully diluted (c)	1.6	25.4	(13.7)	8.9
EPS - (IFRS) (c)	1.6	25.4	(13.7)	8.9
Dividend per share (c)	0.0	2.6	0.0	0.0
Gross Margin (%)	37.8	65.3	19.8	44.7
EBITDA Margin (%)	22.6	54.4	2.7	31.9
Operating Margin (before except.) (%)	3.8	38.8	-14.8	17.6
BALANCE SHEET				
Fixed Assets	35,921	63,952	79,030	83,866
Mine development	12,690	26,554	24,323	20,987
PP&E	12,168	18,074	23,146	25,268
Deferred tax asset	3,025	3,569	3,569	3,569
Tailings inventory	7,409	14,514	20,399	26,150
Other	629	1,241	7,593	7,893
Current Assets	6,202	24,164	13,223	10,409
Inventories	2,510	6,648	10,858	8,945
Receivables	2,341	1,980	2,073	2,185
Cash	1,083	14,916	0	0
Other	268	620	292	(721)
Current Liabilities	(10,502)	(17,193)	(25,196)	(22,599)
Payables	(5,456)	(6,733)	(14,736)	(12,139)
Short term borrowings	0	(6,332)	(6,332)	(6,332)
Other	(5,046)	(4,128)	(4,128)	(4,128)
Long Term Liabilities	(4,317)	(23,758)	(25,158)	(25,158)
Long term borrowings	(3,721)	(22,296)	(22,624)	(23,637)
Other	(596)	(1,462)	(2,534)	(1,521)
Net Assets	27,304	47,165	41,899	46,518
CASH FLOW				
Operating Cash Flow	378	8,661	(2,931)	4,086
Capex	(5,841)	(7,621)	(9,012)	(4,799)
Acquisitions/disposals	0	112	(3,300)	(300)
Equity financing	0	(218)	0	0
Dividends	0	(1,001)	0	0
Other	(284)	(50)	0	0
Net Cash Flow	(5,747)	(117)	(15,244)	(1,013)
Opening net debt/(cash)	(1,056)	2,638	13,712	28,956
Other	2,053	(10,957)	0	0
Closing net debt/(cash)	2,638	13,712	28,956	29,969

Source: Almonty, Edison Investment Research

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