



Kidman Resources Ltd (KDR.ASX)

Bigger, better, richer.

Event:

- Earl Grey JORC Resource upgrade; Earnings changes; PT change.

Investment Highlights:

- **KDR announced an upgrade in size of its Earl Grey JORC Resource to 189Mt from 128Mt, as well as in Li₂O grade to 1.50% from 1.44%.** 91% of the Resources was in Measured and Indicated, with the potential to underpin a mine life over 80 years at 2Mtpa, subject to successful Reserves conversion. We believe the upgrade makes the argument even more compelling for an expanded (e.g. 5Mtpa) mine case. We expect some degree of expansion to be addressed in the upcoming mine DFS.
- **Exploration potential still exists.** The company announced an additional Exploration Target of 20 to 40Mt at 1.3-1.5%. While development and feasibility studies on the mine and refinery have priorities, we expect KDR to still pursue exploration.
- **Our forecast timeline assumptions are approximately in-line with those of KDR.** We expect SQM to still give the project impetus, given the diversification of sovereign risk and shorter lead time to production vs Chilean brine. We expect DFS on the mine and concentrator with maiden Reserves in 2Q CY18e, and the initial refinery study, mine approvals, and decision to mine in late 3Q/early 4Q CY18e.
- **Western Australia Lithium (WAL) JV underway.** The JV was finalised in December 2017 and KDR received US\$5M as part of initial payment for transfer of 50% of Earl Grey. SQM's initial US\$20M payment directly in WAL - which includes KDR's share - have also commenced.

Earnings and Valuation:

- **We forecast underlying NPAT of -\$8.4M and -\$9.3M in FY18e and FY19e (prior -\$14.1M and -\$9.5M)** mostly from slight changes to corporate, studies, and exploration.
- **For FY20e we now forecast NPAT of \$8.1M (previously \$19.5M), the decline mostly due factoring a ramp-up period for initial spodumene production.**
- **NPAT forecasts from FY21e upgraded on higher LCE output.** For FY21e and beyond, we have upgraded our earnings forecasts based on both higher spodumene and lithium carbonate equivalent (LCE) production. These both stem from the higher head grade of the upgraded Earl Grey Resource. We now forecast annual spodumene production of 313kt and LCE production of 41kt LCE in our 2Mtpa base case, an increase of 7% over prior assumptions.
- **Our risked valuation of KDR increases to \$2.72/share from \$1.99, based on the higher long term earnings upgrades from higher LCE and spodumene production, partly offset by higher refinery capex.** We still attribute some value for a risked 5Mtpa expansion case.

Recommendation:

- **We maintain our Buy recommendation and increase our 12-month price target to \$2.72/share from \$1.99, based on our risked valuation.** Catalysts include DFS on mine; maiden JORC Reserve; Initial Refinery study; Mining approvals; Decision to mine; and Commencement of mine development.

Recommendation		Buy
Previous		Buy
Risk		High
Price Target		\$2.72
Previous		\$1.99
Share Price (A\$)		\$ 2.33
ASX Code		KDR
52 week low - high (A\$)		0.335-2.37
Valuation (A\$/share) - risked		\$2.72
Methodology		DCF
Capital structure		
Shares on Issue (M)		351
Market Cap (A\$M)		818
Net Cash/(Debt) (A\$M)		-1
EV (A\$M)		820
Options (M)		48
Share rights (M)		2
Fully diluted EV (\$M)		937
12mth Ave Daily Volume ('000)		3,130

Y/e Jun (A\$M)	2017a	2018e	2019e	2020e
Sales	0.8	0.0	0.0	38.4
Adj EBITDA	-6.7	-8.1	-9.8	14.5
Adj NPAT underlying	-7.2	-8.4	-9.3	8.1
Reported NPAT	-31.3	26.5	29.3	8.1
Adj EPS diluted \$	-0.02	-0.02	-0.02	0.02
PER x diluted	nm	nm	nm	107.6
EV/EBITDA x	nm	nm	nm	35.4

*Adj = underlying FSB estimate

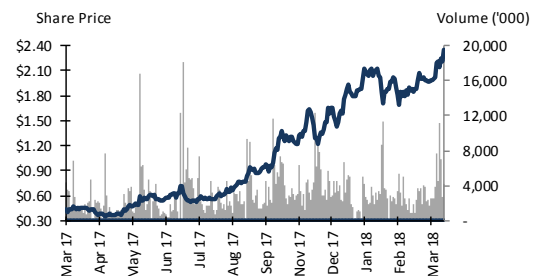
Board

Martin Donohue	Managing Director
John Pizzev	Non-Executive Chairman
Aaron Colleran	Non-Executive Director
David Southam	Non-Executive Director
Brad Evans	Non-Executive Director

Substantial shareholders

EDM Nominees Pty Ltd	9.3%
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Share Price Graph



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The analyst does not own KDR securities.

Foster Stockbroking and associated entities (excluding Cranport Pty Ltd) do not own KDR securities.
Cranport Pty Ltd does not own KDR securities.

This report was prepared by Foster Stockbroking



Kidman Resources (KDR)

Full Year Ended 30 June

Profit and Loss A\$M	2017a	2018e	2019e	2020e
Sales	0.8	0.0	0.0	38.4
Other revenue	0.0	33.5	0.0	0.0
Operating Costs	7.5	8.1	9.8	23.9
Underlying EBITDA	-6.7	-8.1	-9.8	14.5
D&A	0.0	0.1	0.1	3.0
Underlying EBIT	-6.7	-8.1	-9.8	11.5
Net Interest exp / (income)	0.5	0.2	-0.6	0.0
Profit before tax adj	-7.2	-8.4	-9.3	11.5
Tax exp / (benefit)	0.0	0.0	0.0	3.5
Underlying NPAT	-7.2	-8.4	-9.3	8.1
Non-recurring gain/(loss)	-24.1	34.8	38.6	0.0
Reported NPAT	-31.3	26.5	29.3	8.1
Underlying EPS diluted (\$)	-0.02	-0.02	-0.02	0.02

Cashflow A\$M	2017a	2018e	2019e	2020e
Underlying EBITDA	-6.7	-3.0	-5.0	14.5
Change in WC	-3.2	0.0	-2.0	-5.4
Tax paid	0.0	0.0	0.0	-3.5
Other	0.2	-0.1	0.0	0.0
Net interest	0.1	-0.2	0.6	0.0
Share based payments	0.7	0.0	0.0	0.0
Operating Cashflow	-8.9	-3.3	-6.4	5.7

Purchase of PP&E	-0.2	0.0	-25.9	-367.8
Acquisitions	-2.4	0.0	0.0	0.0
Exploration	-8.4	-5.8	-5.8	-5.8
Development	-3.1	0.0	0.0	0.0
Investments	0.1	0.0	0.0	0.0
Other	0.0	39.6	0.0	0.0
Investing Cashflow	-14.0	33.8	-31.7	-373.6

Equity issue	21.0	1.3	0.0	244.5
Debt proceeds	2.1	11.5	11.0	133.0
Debt repayments	-1.0	-11.4	0.0	0.0
Other	-1.4	0.0	0.0	0.0
Financing Cashflow	20.7	1.4	11.0	377.5
Net Cashflow	-2.2	31.9	-27.1	9.5

Balance Sheet A\$M	2017a	2018e	2019e	2020e
Cash	2.6	28.4	1.3	10.8
Receivables	1.8	0.0	0.0	3.2
PPE	0.1	0.1	73.0	437.8
Capitalised exploration	22.1	11.0	11.0	11.0
Other	0.1	4.4	0.0	10.1
Total Assets	26.8	43.9	85.3	472.9

Accounts payable	2.0	0.2	0.5	1.2
Provisions	0.2	0.2	0.8	2.0
Debt	8.4	0.0	0.0	133.0
Other	0.0	0.0	11.2	11.4
Total Liabilities	10.7	0.5	12.5	147.6

Reserves and capital	62.9	63.8	63.8	308.2
Retained earnings	-46.8	-20.4	9.0	17.0
Total Equity	16.1	43.4	72.8	325.3

Capital structure	
Ordinary shares	350.1
Options	49.5
Share rights	1.8
Fully diluted equity	401.4

Financial Metrics	2017a	2018e	2019e	2020e
Sales growth %	nm	nm	nm	nm
EPS growth %	nm	nm	nm	nm
EBITDA margin	nm	nm	nm	38%
EBIT margin	nm	nm	nm	30%
Gearing (ND/ND+E)	27%	-189%	-2%	27%
Interest Cover (EBIT/net int)	nm	nm	17x	-456x
Average ROE %	nm	nm	-16%	4%
Average ROA %	nm	nm	-15%	4%
Wtd ave shares (M)	307	333	350	466
Wtd ave share diluted (M)	307	385	400	515

Sales and earnings multiples	2017a	2018e	2019e	2020e
P/E x	nm	nm	nm	105.5
EV/EBITDA x	nm	nm	nm	35.4
EV/EBIT x	nm	nm	nm	44.7

Company Valuation	A\$M	A\$/sh	A\$M	A\$/sh
Segment	Unrisked A\$M	Unrisked A\$/sh	Risked A\$M	Risked A\$/sh
Mine & concentrator:				
Earl Grey 2Mtpa	524	\$1.01	367	\$0.83
Earl Grey 5Mtpa expansion - incremental vlaue	548	\$1.06	219	\$0.50
Refinery:				
Refinery 41kt LCE - incremental value	286	\$0.55	115	\$0.26
Potential 100kt refinery expansion - incremental	479	\$0.93	192	\$0.43
Yield: Potential higher mine recovery - incremental	688	\$1.33	163	\$0.37
Corporate				
Cash:				
Balance of SQM earn-in payments	88	\$0.17	70	\$0.16
Cash from options exercise	8	\$0.02	7	\$0.02
Cash from future equity raise	244	\$0.47	98	\$0.22
Net cash (debt) at end Dec 17	-1	-\$0.00	-1	-\$0.00
Company Valuation	2823	\$5.46	1201	\$2.72
Ordinary shares now	350		350	
In-money-options	49		45	
Shares from future equity raise	116		46	
Rights vesting at valuation	2		1	
Pro-forma diluted shares M	517		442	

Commodity Assumptions	2017a	2018e	2019e	2020e
Prices				
Spodumene 6% Li ₂ O CFR, US\$/t	695	791	835	747
Lithium carbonate min 99.5%, US\$/t	10,000	16,120	16,023	13,844
A\$:US\$	0.75	0.77	0.76	0.75
Production				
Spodumene 6.0% - external sales, kt	0	0	0	77.2
Lithium carbonate 99.5%, kt	0	0	0	0.0
Costs				
Costs - AISC, US\$/t	0	0	0	297

JORC Resources - Lithium	Ore Mt	Li ₂ O %	Li ₂ O kt	LCE Mt
Earl Grey				
Measured	66	1.58%	1040	2.6
Indicated	106	1.52%	1,610	4.0
Inferred	17	1.11%	190	0.5
Total Resources	189	1.50%	2,840	7.0

Source: Foster Stockbroking estimates.

RESOURCE UPGRADE IN BOTH SIZE AND GRADE

- Kidman Resources Ltd (KDR) announced a 48% upgrade in JORC Resources for Earl Grey from 128Mt to 189Mt. Li₂O grade of the Resource increased as well from 1.44% to 1.50%, resulting in a 54% increase in contained lithia to 2,840kt from 1,839kt. This makes Earl Grey Australia’s largest spodumene resource after Greenbushes.

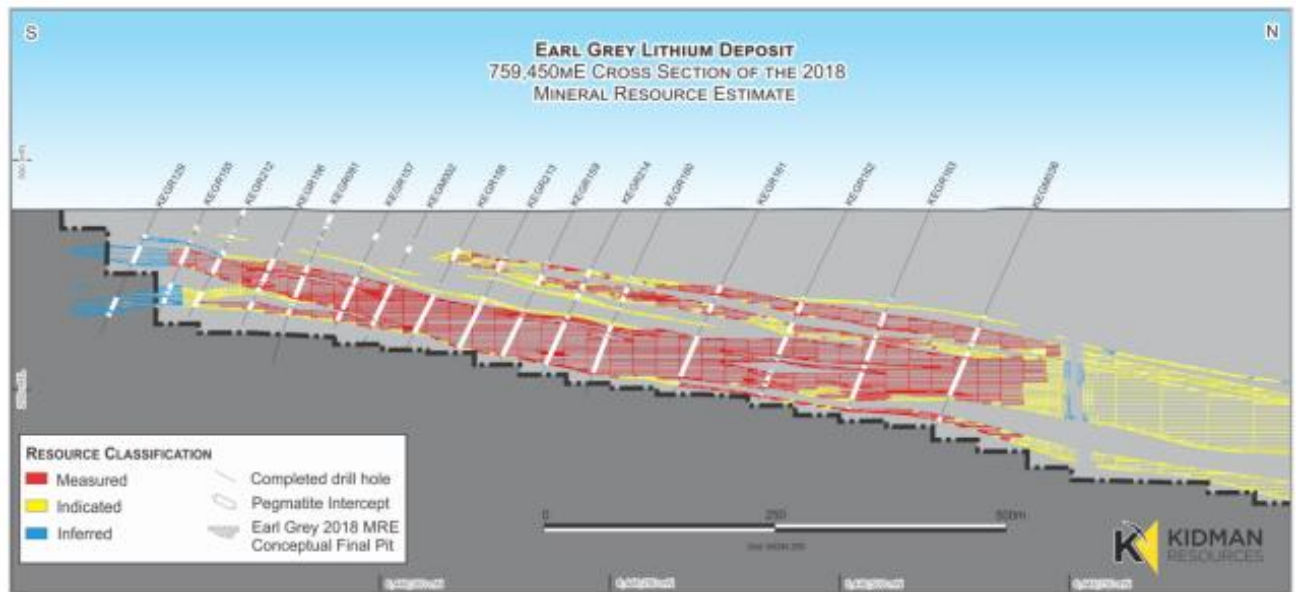
Figure 1: Earl Grey JORC Resource

Category	Ore (Mt)	Li ₂ O (%)	Li ₂ O contained (kt)
Measured	66	1.58	1,040
Indicated	106	1.52	1,610
Inferred	17	1.11	190
Total	189	1.50	2,840

Source: Company.

- 172Mt, or 91%, of the Resource was in the Measured and Indicated category, which should underpin a high maiden JORC Reserve which we expect to be disclosed in the DFS for Earl Grey.
- The increase in resource primarily resulted from extensional drilling at Earl Grey, which lengthened the strike to 2.1km from 1.4km, and to a lesser extent the width (to 1.3km from 900m), with depth of mineralisation up to 300m. Figure 2 shows the typical cross-section continues to exhibit the flat lying nature of the deposit that was also evident in the initial resource estimate, with thicknesses of 15m to 90m.

Figure 2: Earl Grey Cross-Section



Source: Company.

SCALE UP OF MINE EVEN MORE COMPELLING NOW

Potential 2Mtpa mine life of 80+ years based on Measured and Indicated

- The increase in the JORC Resource makes the case even more compelling for the scaling up the mine and concentrator from the 2Mtpa envisioned in last year’s Scoping Study. Based on the Measured and Indicated categories, the Resource underpins a mine life over 80 years at 2 Mtpa mine rate, subject to successful conversion to Reserves.



- We had already thought that the maiden Resource was sufficient enough scale up to 5Mtpa based on NPV. We expect some scale up of the mine and concentrator to be addressed in the DFS. A 5Mtpa rate for example would compress mine life to just over 30 years.

Exploration potential still exists

- In addition to the Resource, KDR also announced an Exploration Target for Earl Grey of 20 to 40Mt at 1.3-1.5% Li₂O, which it will seek to test in further drill campaigns.
- KDR reported that exploration success at Bounty in late 2017 means that this area is no longer suitable for tailings storage, while Texas is another promising area for lithium.
- While feasibility studies and commitment to moving Earl Grey eventually into production are priorities, we believe exploration activity will still continue.

TIMELINE

- Our forecast timelines assumptions are approximately in-line with that of KDR's. The key is that SQM continues to support progress project, despite the agreement reached with Corfo regarding expanding its brine production in Chile. We believe this is still the case, given the diversification of sovereign risk and shorter lead time to production Earl Grey offers in contrast to the brine projects.

CY2018:

- Mine and concentrator DFS/Maiden JORC Reserve – Late 2Q
- Refinery PFS including location decision – 3Q
- Mine & permitting approvals – Late 3Q/early4Q
- Decision to mine and further milestone and JV payments – Late 3Q/early 4Q

CY2019

- Mine and concentrator construction commences - 1Q
- Financing for refinery – 4Q
- Refinery DFS - 3Q/4Q
- Refinery FID – 4Q

CY2020

- Spodumene production – 1Q
- Refinery construction starts – 1Q

CY2021

- First carbonate/hydroxide production – 1Q

JV UNDERWAY

- Finalisation of the JV between SQM and KDR – Western Australia Lithium (WAL) - occurred in December 2017 and KDR received US\$5M milestone initial payment from SQM for transfer of 50% of Earl Grey. Payment of US\$20M by SQM into WAL also commenced, which includes



KDR's share (US\$10M) of funding. The next milestone payment to KDR is US\$25M upon decision to mine, which also triggers further payments by SQM into WAL of US\$60M (including KDR's share of JV payments of US\$30M). We expect decision to mine late 3Q/early 4Q CY18.

EARNINGS FORECASTS - LONG-TERM UPGRADES

- We forecast underlying NPAT of -\$8.4M and -\$9.3M in FY18e and FY19e (prior -\$14.1M and -\$9.5M) mostly from slight changes to corporate and share of funding of exploration and development studies.
- For FY20e we now forecast NPAT of \$8.1M (prior \$19.5M) from initial share of contribution from mining, the decline mostly due to factoring in a ramp-up period for initial Earl Grey spodumene production.

Figure 3: KDR earnings forecasts

Y/e Jun	FY18e			FY19e			FY20e		
	new	old	chng	new	old	chng	new	old	chng
Sales	0.0	0.0	0%	0.0	0.0	0%	38.4	68.4	-44%
Other revenue	33.5	40.0	-16%	0.0	0.0	0%	0.0	0.0	0%
Operating costs	8.1	13.5	-40%	9.8	10.0	-2%	23.9	37.4	-36%
EBITDA	-8.1	-13.5	-40%	-9.8	-10.0	-2%	14.5	31.0	-53%
DA	0.1	0.2	-75%	0.1	0.2	-75%	3.0	3.2	-5%
EBIT	-8.1	-13.7	-41%	-9.8	-10.2	-4%	11.5	27.8	-59%
Net interest	0.2	0.4	-41%	-0.6	-0.8	-25%	0.0	-0.1	-53%
PBT	-8.4	-14.1	-41%	-9.3	-9.5	-2%	11.5	27.9	-59%
Tax	0.0	0.0	0%	0.0	0.0	0%	3.5	8.4	-59%
NPAT adj	-8.4	-14.1	-41%	-9.3	-9.5	-2%	8.1	19.5	-59%
Non-recurring	34.8	43.5	-20%	38.6	38.6	0%	0.0	0.0	0%
NPAT reported	26.5	29.4	-10%	29.3	29.1	1%	8.1	19.5	-60%

Source: Foster Stockbroking estimates

Earnings in later years upgraded on higher spodumene and LCE production

- However our NPAT forecast in later years (FY21e onwards – see Figure 5) have increased due to both higher annual spodumene mine output and carbonate production from the refinery. These both stem from the higher Li₂O head grade of Earl Grey resource – we now assume 1.50% average Li₂O head grade vs prior assumption of 1.40%. Our long term LCE production increases 8% to 40kt from 37kt previously, with spodumene output similarly increasing to 309ktpa vs 288ktpa previously. Our earnings forecast are based on 2Mtpa operation which remains our base case.

Figure 4: Earl Grey production assumptions (2Mtpa base case)

Parameter	New	Old	Chng
Head grade Li ₂ O %	1.50%	1.40%	7%
Spodumene production ktpa	309	288	7%
LCE production ktpa	40	37	8%

Source: Foster stockbroking estimates.

- We have also incorporated our updated commodity forecasts (Figure 6).

Figure 5: Earl Grey Base Case 2Mt/pa Integrated Mine & Refinery Cashflows FY18-FY23e (100%)

Y/e June	Unit	2018e	2019e	2020e	2021e	2022e	2023e
Commodity assumptions:							
Li ₂ CO ₃ min 99.5%	US\$/t	16,120	16,023	13,844	12,199	11,331	11,558
Spodumene SC6.0	US\$/t	791	835	747	682	651	664
A\$	US\$	0.77	0.76	0.75	0.74	0.74	0.74
Spodumene external sales SC6.0	kt	0	0	77	154	0	0
Spodumene refinery feed SC6.0	kt	0	0	0	154	309	309
Li refinery recovery	%	0%	0%	0%	87%	87%	87%
Li ₂ CO ₃ min 99.5% produced	kt	0	0	0	20	40	40
Cashflow:							
Spodumene SC6.0 ext sales	A\$M	0	0	77	142	0	0
Li ₂ CO ₃ min 99.5% sales	A\$M	0	0	0	328	610	622
Total sales (A)	A\$M	0	0	77	471	610	622
Spodumene costs	A\$M	0	0	29	45	91	92
Conversion costs	A\$M	0	0	0	72	147	150
Freight	A\$M	0	0	0	1	1	1
Royalty	A\$M	0	0	0	16	31	31
Total cash costs (B)	A\$M	0	0	28	134	269	275
EBITDA	A\$M	0	0	49	336	341	348
Capex (C)	A\$M	0	146	736	11	11	11
Chng In Working Capital (D)	A\$M	0	0	-2	-26	-12	-1
Tax (E)	A\$M	0	0	3	89	90	92
Net Free Cashflow (A-B-C+D-E)	A\$M	0	-146	-693	211	228	244
All-in-sustaining costs	US\$/t	-	-	-	5,382	5,201	5,305

Source: Foster Stockbroking estimates.

Figure 6: Commodity forecast changes

Y/e June	FY18e	FY19e	FY20e	FY21e	LT
Spodumene SC6.0 US\$/t - new	791	835	747	682	651
Old	791	768	712	667	658
Chng	0%	9%	5%	2%	-1%
Lithium carbonate BG US\$/t	16,120	16,023	13,844	12,199	11,331
Old	15,531	17,501	15,117	12,769	10,914
chng	4%	-8%	-8%	-4%	4%
AS:US\$	0.77	0.76	0.75	0.74	0.74
Old	0.76	0.76	0.75	0.75	0.75
Chng	1%	0%	0%	-1%	-1%

Source: Foster Stockbroking estimates.

**VALUATION \$2.72/SHARE (PRIOR \$1.99)****Resource upgrade drives valuation increase**

- Our risked valuation of KDR has increased to \$2.72/share from \$1.99/share, mostly based on the JORC Resource upgrade in both size and grade which has extended Earl Grey's mine life as well as its annual spodumene and LCE production. These have been partly offset by forecast higher capex for the refinery. We continue to attribute some value to the expansion case of both the mine/concentrator and the refinery. We believe this is more probable post the Resource upgrade.
- Our unrisked valuation is \$5.46/share. This includes an unrisked 5Mtpa expanded mine, expanded refinery of >100ktpa of LCE, and lithia recovery of 85%.

Figure 7: KDR Valuation

Segment	Unrisked A\$M	Unrisked A\$/sh	Risked A\$M	Risked A\$/sh	1- Risk factor
Mine & concentrator:					
Earl Grey 2Mtpa	524	\$1.01	367	\$0.83	70%
5Mtpa expansion - incremental value	548	\$1.06	219	\$0.50	40%
Refinery:					
Refinery 41kt LCE - incremental	286	\$0.55	115	\$0.26	40%
Potential 100kt refinery expansion - incremental	479	\$0.93	192	\$0.43	40%
Yield: Potential higher recovery - incremental	688	\$1.33	163	\$0.37	24%
Corporate	-41	-\$0.08	-29	-\$0.06	70%
Cash:					
Balance of SQM earn-in payments	88	\$0.17	70	\$0.16	80%
Cash from options exercise	8	\$0.02	7	\$0.02	90%
Cash from future equity raise	244	\$0.47	98	\$0.22	40%
Net cash (debt) at end Dec 17	-1	-\$0.00	-1	-\$0.00	100%
Company Valuation	2,823	\$5.46	1,201	\$2.72	43%
Ordinary shares now	350		350		100%
In-money-options	49		45		90%
Shares from future equity raise	116		46		40%
Share rights vesting at valuation	2		1		47%
Pro-forma diluted shares M	517		442		85%

Source: Foster Stockbroking estimates.

RECOMMENDATION – MAINTAIN BUY, 12-MONTH PRICE TARGET \$2.72/SHARE

- We maintain our Buy recommendation on KDR and lift our 12-month price target to \$2.72/share from \$1.99/share, based on our risked valuation. Catalysts over the next 12 months for the share price include:
 - Mine and concentrator DFs and maiden Reserves.
 - Mining approvals;
 - Decision to mine;
 - Mine construction; and
 - Initial study on refinery.



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