

Element 25 Limited

A Manganese-rich Opportunity

October 2021

Recommendation: BUY

- Australian manganese producer self-funded to triple production at a 300%+ IRR
- PFS on high-purity manganese for battery markets due this quarter
- High quality management team with a history of delivery

ASX: E25

Share Price: \$1.91

Target Price: \$3.98

M/Cap.: \$282.7M

Valuation: \$3.98/share

Valuation: \$788M

Shares/options: 148.8

Monthly T/over: \$16.2M



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Petra Capital Pty Ltd

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Element 25 Limited (E25)

Buy

Share Price: A\$1.91

A manganese efficient opportunity

Target Price: A\$3.98

Element 25 Ltd (E25) is an ASX-listed manganese concentrate producer through its 100% owned Butcherbird project in the Pilbara, Western Australia. Management have delivered Butcherbird into production this year. With organic, self-funded expansions over the next 12 months to triple output, we see strong earnings growth. In addition, E25 concentrate has been confirmed to be suitable for upgrading to high purity manganese sulphate (HPMSM) and studies are underway to determine the economics of investing in downstream production for battery material markets. With supply constraints indicating a tight manganese market, we see E25 re-rating as expansions are completed and the pathway to supplying battery material markets becomes clearer. We initiate coverage with a BUY and A\$3.98/sh price target (1xP/NPV₈).

A simple, scalable project in a tier one jurisdiction

- E25 delivered first Mn conc shipments from the 300ktpa Butcherbird Stage 1 to customers in the Sept Q 2021
- The open pit operation is shallow and mainly free dig, with the 13 year Reserve life likely to grow materially
- Concentrate is produced via a simple crush/screen/sort circuit and is trucked to Port Hedland for export via a sealed highway that passes through the mining lease
- Production expansion to 1Mtpa is expected by 1H 2022 and, at a low capex of A\$20m, it will be self-funded
- The Mn concentrate operation has EBITDA margins of 40% with annual EBITDA moving from an average of A\$18m for Stage 1 to A\$92m post expansion from FY24

Battery market exposure will add further value

- Manganese is the cheapest and most abundant of the NMC cathode materials (nickel/manganese/cobalt). Use is increasing as other materials become difficult to source
- High purity manganese (HPMSM) is required for cathode use. E25's concentrate is suitable as feedstock for an upgrade facility, with a PFS to be released this quarter
- We incorporate a 50ktpa HPMSM facility in our base case, with A\$200m capex generating A\$50m/yr EBITDA from early 2024; additional circuits may be added in time

Significant upside to our A\$3.98/sh price target

- Our fully diluted A\$3.98/sh target is based on 1.0x NPV₈
- We assume average benchmark manganese prices of US\$6.20/dmtu and a 0.75 AUDUSD

Key Dates Ahead

- Dec 2021 – Stage 1 production run-rate achieved
- Dec 2021 – PFS on manganese sulphate expected
- 1H 2022 – Expansion to 1Mtpa Mn conc complete
- 1H 2024 – First production from HPMSM plant

Company Data

Shares – ordinary (M)	148.8
Market capitalisation (\$M)	282.7
12 month low/high (\$)	0.73/ 2.9
Average monthly turnover (\$M)	16.2
GICS Industry	Metals & Mining

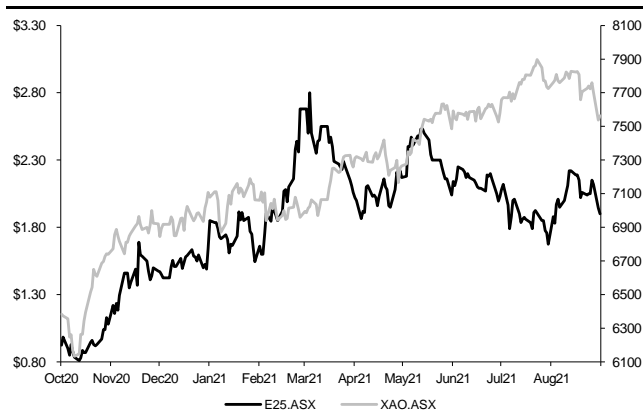
Financial Summary (fully diluted/normalised)

Year end June	2021A	2022F	2023F	2024F	2025F
Revenue (\$M)	1.3	59.8	163.7	227.2	310.6
Costs (\$M)	7.5	55.4	106.3	134.8	181.5
EBITDA (\$M)	-6.3	4.4	57.4	92.4	129.2
NPAT (\$M)	-6.5	4.3	40.9	62.5	80.1
EPS (¢ps)	-4.4	2.9	25.0	37.6	48.2
EPS growth (%)	72.0	249.3	753.9	50.5	28.3
PER (x)	-43.6	65.2	7.6	5.1	4.0
Op. Cashflow (\$M)	-3.7	7.1	57.9	67.6	98.8
OCFPS (¢ps)	-2.5	4.8	38.9	45.4	66.4
POCFPS (x)	-77.3	40.0	4.9	4.2	2.9
EV (\$M)	249	244	233	281	216
EV / EBITDA (x)	-39.7	55.4	4.1	3.0	1.7
Payout ratio (%)	0.0	0.0	0.0	0.0	0.0
Dividends (¢ps)	0.0	0.0	0.0	0.0	0.0
Yield (%)	0.0	0.0	0.0	0.0	0.0
Franking (%)	0.0	0.0	0.0	0.0	0.0

Board

Director	Position	Executive	Independent
Seamus Cornelius	Chairman	No	Yes
Justin Brown	MD	Yes	No
John Ribbons	Director	No	Yes

E25 – performance over one year



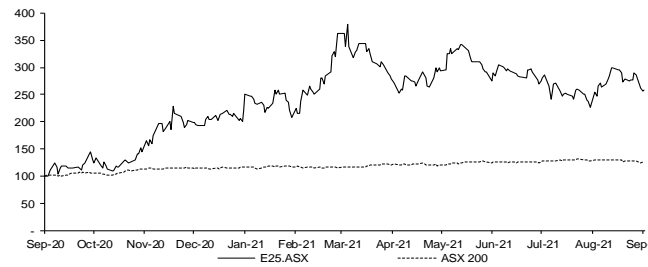
Analysis

Element 25 Limited (E25)

Year end 30 June

Recommendation

Price	\$	1.91
Target Price (12-month)	\$	3.98
Upside / (Downside)	%	109%
52 week high / low	\$	2.8 - 0.74
Market capitalisation	\$m	283
Shares on issue	no.	149
Options	no.	6
Shares on issue (diluted)	no.	198



PROFIT & LOSS		2021A	2022E	2023E	2024E	2025E
Revenue	\$M	1	60	164	227	311
Operating Costs	\$M	(2)	(49)	(100)	(129)	(175)
Exploration	\$M	(2)	(2)	(2)	(2)	(2)
Other	\$M	(4)	(4)	(4)	(4)	(4)
EBITDA	\$M	(6)	4	57	92	129
Dep. & Amort.	\$M	(0)	(1)	(2)	(3)	(12)
EBIT	\$M	(6)	4	55	90	117
Net Interest	\$M	(0)	1	1	(1)	(3)
Pre-Tax Profit	\$M	(6)	4	57	89	114
Tax	\$M	-	-	(16)	(27)	(34)
Net Profit	\$M	(6)	4	41	62	80
Abnormal	\$M	-	-	-	-	-
Reported Profit	\$M	(6)	4	41	62	80

ASSUMPTIONS		2021A	2022E	2023E	2024E	2025E
AS\$/US\$ exchange rate	\$	0.75	0.76	0.76	0.75	0.75
Mn Conc ref price (44%)	US\$/dmu	6.35	5.40	5.80	6.10	6.20
Realised price	A\$/dmu		6.06	6.47	6.81	6.94
High Purity Mn price	US\$/t	1,500	1,558	1,673	1,760	1,788

BUTCHERBIRD MINE LIFE

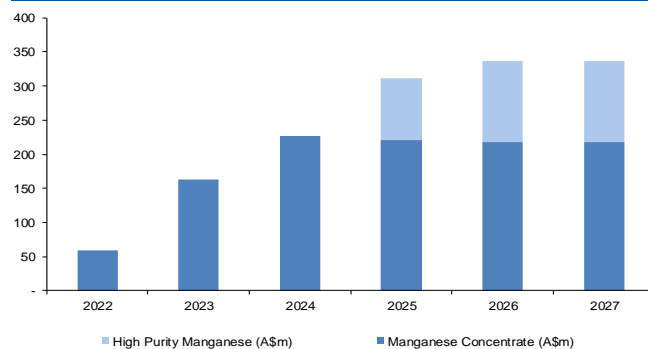
	Contained Mn	Grade (%)	Years
Reserves	4.3	10.3%	13
Resources	21.6	10.0%	65
Petra Mining Inventory	6.0	10.3%	20

PRODUCTION & COSTS

		2021A	2022E	2023E	2024E	2025E
Tonnes processed	Mtpa		1.2	2.9	3.9	3.9
Grade	g/t		10.3%	10.3%	10.3%	10.3%
Recovery	%		83%	83%	83%	83%
Mn Conc Production	kt	-	297	755	1,007	1,007
Mn Conc Sales	kt	-	297	755	1,007	962
HP Mn Production	kt	-	-	-	-	38

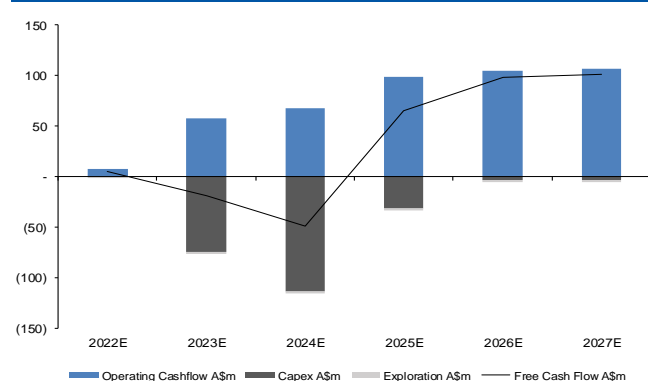
CASH FLOW		2021A	2022E	2023E	2024E	2025E
Revenue	\$M	1	60	164	227	311
Costs	\$M	(5)	(53)	(104)	(133)	(179)
Tax Payable	\$M	-	-	(3)	(26)	(30)
Other	\$M	1	1	(1)	(27)	(32)
Operating Cashflow	\$M	(4)	7	58	68	99
Capex	\$M	(22)	-	(75)	(114)	(32)
Exploration	\$M	(2)	(2)	(2)	(2)	(2)
Acquisitions	\$M	-	-	-	-	-
Other	\$M	(0)	-	-	-	-
Investing Cashflow	\$M	(24)	(2)	(77)	(116)	(34)
Equity Issues	\$M	60	-	30	-	-
Debt Raised / (repaid)	\$M	-	-	-	70	-
Free Cashflow	\$M	(28)	5	(19)	(49)	65
Surplus Cash Flow	\$M	32	5	11	21	65

REVENUE BY PRODUCT



BALANCE SHEET		2021A	2022E	2023E	2024E	2025E
Cash	\$M	35	40	51	72	137
Other Current	\$M	10	10	12	38	68
Total Current	\$M	44	49	63	110	205
PP&E & Exploration	\$M	23	22	95	207	226
Other	\$M	2	2	2	2	2
Total NC Assets	\$M	25	24	97	209	228
Total Assets	\$M	69	73	160	319	434
Current Liab	\$M	6	6	6	6	6
Non Current Liab	\$M	1	1	1	71	71
Total Liabilities	\$M	6	6	6	76	76
Net Assets	\$M	62	67	153	243	357
Equity	\$M	62	67	153	243	357
Total Debt	\$M	-	-	-	70	70
Net Debt	\$M	(35)	(40)	(51)	(2)	(67)

CASH GENERATION



RATIO ANALYSIS		2021A	2022E	2023E	2024E	2025E
EPS	¢	(4.4)	2.9	25.0	37.6	48.2
PER	x	(43.6)	65.2x	7.6x	5.1x	4.0x
EPS Growth	%	72%	249%	754%	50%	28%
EV/EBITDA	x	(39.7)	55.4x	4.1x	3.0x	1.7x
EV/OCF	x	(67.8)	34.3x	4.0x	4.2x	(6.7)
FCFPS	¢	(18.7)	3.4	(12.9)	(32.7)	43.9
FCF Yield	%	(10%)	2%	(7%)	(17%)	23%
DPS	¢	-	-	-	-	-
Yield	%	-	-	-	-	-
Franking	%	-	-	-	-	0%
Payout Ratio	%	-	-	-	-	-
Gearing D/E	%	-	-	-	29%	20%
Interest Cover	x		n.m.	n.m.	140	45
EBITDA Margin	%		7%	35%	41%	42%
EBIT Margin	%		6%	34%	40%	38%
Return On Assets	%		17%	58%	43%	52%
Return On Equity	%		7%	27%	26%	22%
Eff Tax rate (cash tax)	%		-	4%	29%	30%

VALUATION (8% real discount rate)

	A\$m	A\$/Sh	%
Butcherbird Manganese Conc	604	3.05	
High Purity Manganese	178	0.90	
Exploration	10	0.05	
Net Cash	35	0.18	
Corporate	(39)	(0.20)	
Group NPV	788	3.98	0.48

Source: Petra Capital

Executive Summary

A manganese producer in a tier 1 jurisdiction

Element 25 Limited (E25) is an ASX-listed, manganese producer through its Butcherbird project, located in the Pilbara region of Western Australia. Butcherbird's Dec 2020 PFS outlined a staged project capable of producing 1Mtpa of manganese concentrate at costs of US\$2.65/dmtu. The company has successfully commissioned Stage 1 of the project, with two maiden shipments sold in the Sept Q 2021. We expect the A\$20m in additional expansion capital to achieve a 1Mtpa production rate by 2023, to be self-funded. The Reserve underpins a 13-year life at these rates, although the ultimate mine life is expected to be longer given the Reserve represents just 20% of the Resource base. Now the asset is in production, management focus is on execution of production expansion as well as defining the pathway to high purity manganese sulphate production for use in the battery sector.

Strong economics driven by a simple operation near great infrastructure

The geology of Butcherbird is simple. The deposit occurs as a wide ore body close to surface, with a high proportion of low cost free dig mining and a strip ratio of 0.36:1. Concentrate production is both simple and low cost, with Stage 1 capex of A\$20m and only a further A\$20m required to expand production to 1Mtpa of manganese concentrate. This asset will generate over A\$200m in revenue at ~40% EBITDA margins. The mining lease is intersected by the Great Northern Highway, which has sealed access all the way to Port Hedland, where E25 ships concentrate to its customers under existing offtake agreements.

A\$3.98/sh Price Target underpinned by low risk expansions

Our Buy recommendation and A\$3.98/sh price target is set in-line with our fully diluted NPV at an 8% discount rate. This assumes average life-of-mine manganese prices of US\$6.20/dmtu (44% benchmark price) and \$30m of new equity funding at \$1.71/sh.

Our A\$716m valuation for E25's manganese business is primarily attributed to E25's manganese concentrate business (A\$604m). Our estimates largely reflect the Dec 2020 PFS metrics, after accounting for recent cost inflation in shipping and transport. Management has demonstrated an ability to deliver to guidance and the concentrate business alone represents A\$3.05/sh, or 60% upside from the current share price. The current share price is factoring in no production growth, which provides a material opportunity for investors given the high confidence of the Reserves, the proven product quality and path to market, as well as scalable infrastructure with minimal expansion capital.

Battery materials exposure could deliver meaningful upside

Manganese is the cheapest and most abundant of the NMC cathode materials (nickel, manganese and cobalt). These types of cathodes are in the majority of battery designs expected to be in production over the next two decades. There are sufficient manganese units in global supply to satisfy cathode demand however there is insufficient High Purity Manganese Sulphate Monohydrate (HPMSM) facilities.

When E25 expands production above 400ktpa, it will have excess material above its offtake arrangements. The company is investigating investing in a high purity manganese facility that would be fed by Butcherbird concentrate. We expect a PFS reviewing the potential for a 50ktpa HPMSM facility using E25 ore by the end of 2021. This could lead to a DFS during 1H 2022 and first production in 2024. Our base case forecasts assume a 50ktpa HPMSM operation is operational by 2024, for A\$200m in capital and generating operating margins of 45%. We include a A\$178m valuation for a HPMSM operation in our base case forecasts, noting the large resource base and modular nature of these plants could lead to E25 growing this business, as battery growth drives increased Mn sulphate demand..

Manganese supply becoming tight in the medium term

Manganese is the fourth most used metal globally, with the majority of mined material used to strengthen steel. Australian ore production has declined over the last two years, while South Africa, the largest global producer, has remained steady. Our review of manganese markets leads us to conclude that large scale mines in tier one jurisdictions are in production decline and Butcherbird manganese is likely to be in strong demand over the medium to long term, especially as battery demand grows materially.

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