

# VENTUREX RESOURCES (VXR)

**A tough 12 months, but fundamentals intact**

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We say

Price

Target

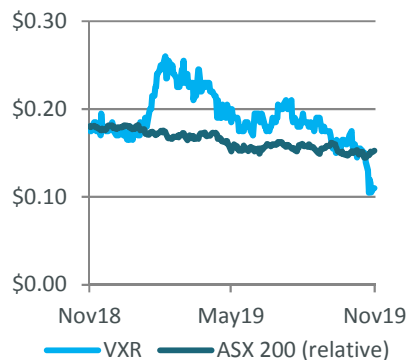
Strategic Target

# BUY

# 0.11 0.50 0.70

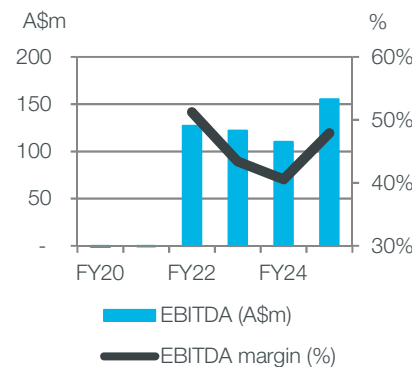
Venturex recently surprised the market when the MD resigned for personal reasons and the stock sold off sharply. While the news was disappointing, in our view the strong fundamentals of the Sulphur Springs project remain intact. The stock has had a tough ~12 months, largely due to the China/US trade war and slower than expected permits. But encouraging progress was made during the quarter and EPA Board feedback is expected within ~4-6 weeks. We ease our Target to 50c (70c).

## SHARE PRICE CHART



Source: IRESS, Blue Ocean Equities

## FORECAST EBITDA (A\$m) & MARGIN (%)



Source: Company, Blue Ocean estimates

## COMPANY DATA & RATIOS

Enterprise value	\$29m
Diluted market cap*	\$31m
Diluted shares*	286m
Free float	81%
12 month price range	\$0.27-0.11
GICS sector	Materials
Northern Star 19%, Board & Management hold ~5% (FD) . *Diluted for 6.4m options	

## IMPLIED RETURN

Implied all-in return	~350%
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## PROGRESS ON PERMITS FUNDAMENTALS INTACT

In VXR's Sept Q report on 31 Oct, the company stated the Environmental impact assessment for Sulphur Springs "progressed during the quarter".

On 19 Sept the EPA accepted the company's Environmental Review Documents (ERD) and is now preparing a draft assessment report. Feedback from the EPA Board is expected within 4-6 weeks. We provide more detail on p2.

Based on DFS assumptions, at spot prices we estimate VXR's 100%-owned Sulphur Springs project in WA has:

- NPV post tax of A\$263m
- IRR post tax of ~39%

At US\$3.00/lb copper, these metrics improve to:

- NPV post tax of A\$382m
- IRR post tax of ~50%

## EASE TARGET TO 50c

We reduce our Price Target to 50c (previously 70c) and change our rating to Buy (from Top Pick). The key change to our valuation is a lower price assumption for the company's major raising (see p4), resulting in higher dilution accounted for by a 60% discount to our NPV for Sulphur Springs (previously 50%). We have also reduced our long term copper price to US\$3.00/lb (US\$3.20/lb) offset by a lower long term A\$/US\$ of 0.68 (prev. 0.70).

## PROMISING PROGRESS ON PERMITS

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Venturex has had a tough ~12 months, largely due to:

- Soft base metals prices due to the China/US trade war
- Slower than expected permits
- The recent resignation of the MD

But despite these headwinds, the company made encouraging progress on permits during the September quarter, as highlighted in the extract below:

*Environmental impact assessment of the Sulphur Springs Project progressed during the quarter.*

*A multi-agency meeting in August, called by the EPA Chairperson and attended by Company representatives, proved constructive. The key characteristics of the project were discussed and a pathway to finalise the environmental review documentation for completion of the assessment by the EPA was set out.*

*Subsequent to that meeting, on the 19th September 2019, the EPA accepted the Company's Environmental Review Document (ERD) and is now preparing a draft assessment report. The EPA Board considered the proposal at its meeting on 24 October 2019 and feedback is expected within the next 6-8 weeks.*

As we understand it, there were a number of iterations involved in preparing the Environmental Review Document (ERD) which has now been finalised – we regard as an important step forward.

Getting the proposal in front of the EPA Board also took longer than expected, so again, we regard this as another promising step forward.

## FUNDAMENTALS INTACT

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We continue to believe Venturex's 100%-owned Sulphur Springs project in WA remains one of the best undeveloped base metal projects in Australia.

Based on DFS assumptions, at spot prices we estimate VXR's 100%-owned Sulphur Springs project in WA has:

- NPV post tax of A\$263m
- **IRR post tax of ~39%**

At US\$3.00/lb copper, these metrics improve to:

- NPV post tax of A\$382m
- **IRR post tax of ~50%**

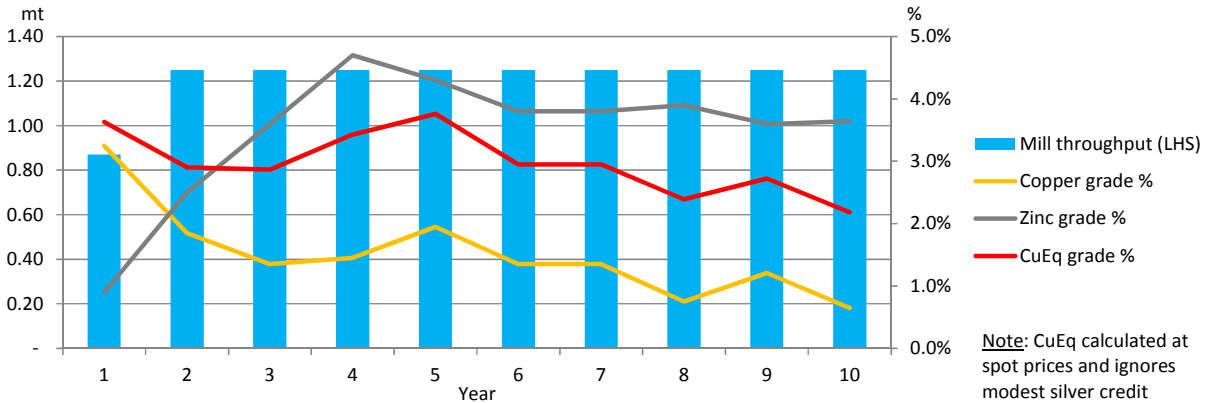
In a low-yield world, we believe the potential returns of Sulphur Springs are *highly* appealing.

For context, Sulphur Spring's projected IRRs are *much* higher than most comparable-sized mining projects, which is primarily driven by the Sulphur Springs ~3% copper equivalent grade.

## THE SULPHUR SPRINGS CU/ZN PROJECT, WA

The key driver behind Sulphur Spring compelling economics is *grade* – the project has very high CuEq grade of ~3% for most of the mine life – refer to the red line in the chart below. These grades are particularly lucrative over the first ~4.5 years during the open pit operation.

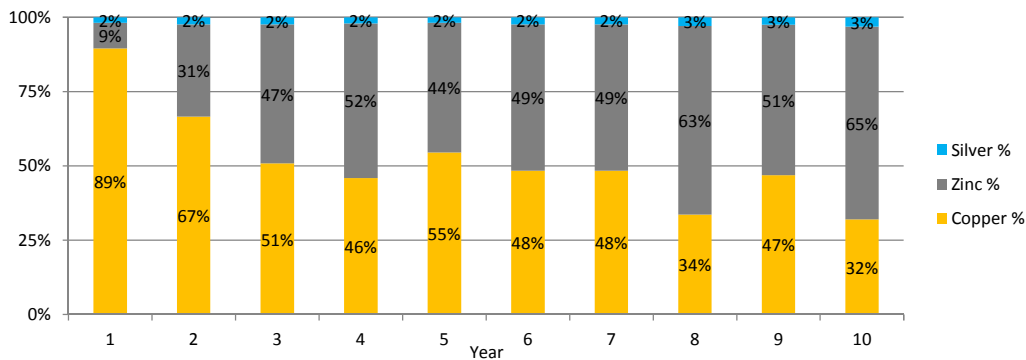
### Copper Equivalent Grades of ~3% or better for most of the mine life



Source: Company, Blue Ocean estimates

The revenue split for Sulphur Springs is ~50/50 copper/zinc over the mine life, but higher copper in the early years as illustrated in the chart below.

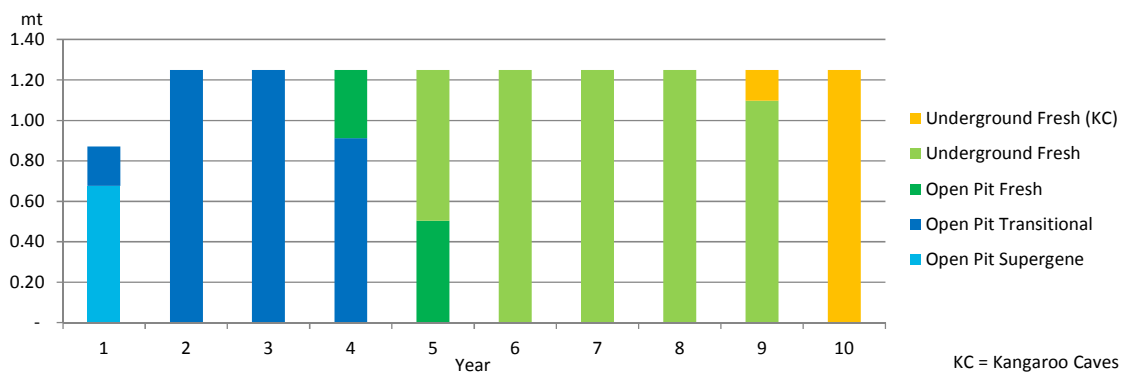
### Revenue split by metal over the mine life



Source: Company, Blue Ocean estimates

Sulphur Springs is set to process ~676kt of supergene copper ore in the first 12 months (~5% of the mining inventory in the DFS) followed by transition ore for ~3 years and fresh ore thereafter.

### Mill Throughput by Ore Type



Source: Company, Blue Ocean estimates

## FUNDING SULPHUR SPRINGS

The DFS for Sulphur Springs was completed on 10 October 2018 and estimated initial capex at A\$169m. Our funding assumptions for Sulphur Springs are outlined below:

### Funding Assumptions

Funding Uses	A\$m
Initial Capex	170
Working capital & other	30
<b>Total</b>	<b>200</b>

Funding Sources		A\$m
Equity	50%	100
Trafigura Debt	50%	100
<b>Total</b>		<b>200</b>

Source: Company, Blue Ocean Equities

In August 2019, Venturex signed a term sheet with Trafigura for A\$100m debt funding and offtake<sup>1</sup>.

The company is also confident its major shareholder in Northern Star (ASX:NST), will provide its pro-rata 19.9% share of the project equity when the time comes to build Sulphur Springs.

Our previous valuation of Sulphur Springs assumed a major raising price of 25c, but since then the stock has been under pressure and last closed at 11c.

We believe the stock can recover as the key de-risking milestones come through, particularly the environmental approvals, which the company expects near-term.

Our revised valuation assumes the major raising is undertaken at 15c, however if the stock can recover more, our valuation and Price Target would improve sharply, as set out in the sensitivity table below:

### Value per share sensitivity to major raising price

Commodity Price & FX Scenario	Copper US\$/lb	Zinc US\$/lb	FX A\$/US\$	NAV/share A\$/share	Major Raising Price			
					0.10	0.15	0.20	0.25
Spot	2.64	1.08	0.679	Spot	0.29	0.39	0.47	0.54
DFS	2.86	1.20	0.72	DFS	0.32	0.43	0.52	0.60
BOEQ	3.00	1.20	0.68	BOEQ	0.38	0.51	0.62	0.71

Source: Company, Blue Ocean Equities

<sup>1</sup> Detailed terms of Trafigura debt and offtake in VXR's release, available here: <https://wcsecure.weblink.com.au/pdf/VXR/02130406.pdf>

## PRICE TARGET & RATING

We reduce our Price Target for Venturex to 50c (from 70c) based on:

- A higher 60% discount to NPV (previously 50%) to accommodate development risks and higher potential dilution compared to when we last published
- A largely unchanged un-risked NPV for Sulphur Springs of ~A\$370m using DFS operating assumptions (but excluding Kangaroo Caves), based on unchanged Blue Ocean commodity price forecasts of:
  - US\$3.00/lb copper (previously US\$3.20/lb)
  - US\$1.20/lb zinc (unchanged)
  - 0.68 A\$/US\$ (previously 0.70)
  - a 10% nominal discount rate (unchanged)

It is important to flag that we intend to reduce our discount to NPV if the company's share price rallies to materially higher levels, resulting in a less dilutive major raising, as outlined in the sensitivity table on page 4 of this report.

We have also pushed out our assumed development timetable for Sulphur Springs by ~6 months, and now assume the ~15 month construction period begins in Q2 CY20.

We move our rating to Buy (previously Top Pick) and our new 50c Price Target (previously 70c) represents an implied return of over 350%.

## STRATEGIC TARGET

We derive our \$0.70 Strategic Target for Venturex assuming the company's share price rallies to ~25c or higher over the next few months, and the company is able to undertake its major raising at ~25c or higher.

It is important to note that our Strategic Target does *not* account for higher copper or zinc prices *or* for further exploration success at Sulphur Springs, which could lead to a longer mine life and a higher Price Target.

## KEY RISKS

Venturex is exposed to all the normal risks associated with developing and operating mining projects, including permitting, funding and construction risk, as well as normal project ramp up and commissioning risks.

Assuming Venturex makes the transition into production, its revenues will be derived from the sale of copper and zinc concentrates (and a modest silver credit). Fluctuations in the prices of these commodities as well as the Australian dollar could impact the company's reported cash flow (in A\$), profitability and share price.

As Venturex's Sulphur Springs project is based in Western Australia, an investment in Venturex also carries Australian sovereign risk. However, it is worth noting that Australia is considered materially lower sovereign risk than many of the other jurisdictions around the world.

**MODEL SUMMARY: FINANCIALS & VALUATION**

Macro Assumptions	FY19A	FY20E	FY21E	FY22E	FY23E
Exchange Rate (A\$/US\$)	0.72	0.68	0.68	0.68	0.68
Copper Price (US\$/lb)	2.79	2.90	3.00	3.00	3.00
Zinc Price (US\$/lb)	1.21	1.20	1.20	1.20	1.20

Profit & Loss (A\$m)	FY19A	FY20E	FY21E	FY22E	FY23E
Revenue	-	-	-	248	281
Operating Costs	-	-	-	(115)	(154)
<b>Operating Profit</b>	-	-	-	<b>132</b>	<b>127</b>
Corporate & Other	(2)	(4)	(4)	(5)	(5)
Exploration Expense	(0)	(0)	(0)	(0)	(0)
<b>EBITDA</b>	<b>(2)</b>	<b>(4)</b>	<b>(4)</b>	<b>127</b>	<b>122</b>
D&A	(0)	(0)	-	(28)	(24)
<b>EBIT</b>	<b>(2)</b>	<b>(5)</b>	<b>(4)</b>	<b>99</b>	<b>98</b>
Net Interest Expense	(0)	-	-	(8)	(2)
<b>Pre-Tax Profit</b>	<b>(3)</b>	<b>(5)</b>	<b>(4)</b>	<b>91</b>	<b>96</b>
Tax Expense	-	-	-	(27)	(29)
<b>Underlying Profit</b>	<b>(3)</b>	<b>(5)</b>	<b>(4)</b>	<b>63</b>	<b>67</b>
Significant Items (post tax)	-	-	-	-	-
<b>Reported Profit</b>	<b>(3)</b>	<b>(5)</b>	<b>(4)</b>	<b>63</b>	<b>67</b>

Cash Flow (A\$m)	FY19A	FY20E	FY21E	FY22E	FY23E
Operating Cashflow	(1)	(4)	(4)	127	122
Tax	-	-	-	(13)	(28)
Net Interest	(0)	-	-	(8)	(2)
<b>Net Operating Cash Flow</b>	<b>(1)</b>	<b>(4)</b>	<b>(4)</b>	<b>106</b>	<b>92</b>
Exploration	(3)	(4)	(4)	(4)	(4)
Capex	(1)	(43)	(128)	(1)	(3)
Acquisitions / Disposals	0	-	-	-	-
Other	(0)	-	-	-	-
<b>Net Investing Cash Flow</b>	<b>(4)</b>	<b>(47)</b>	<b>(132)</b>	<b>(5)</b>	<b>(7)</b>
Equity Issue	6	100	-	-	-
Borrowing / Repayments	2	-	100	(50)	(50)
Dividends	-	-	-	(10)	(19)
Other	0	-	-	-	-
<b>Net Financing Cash Flow</b>	<b>8</b>	<b>100</b>	<b>100</b>	<b>(60)</b>	<b>(69)</b>
Change in Cash Position	2	49	(36)	41	16
FX Adjustments	-	-	-	-	-
<b>Cash Balance</b>	<b>5</b>	<b>54</b>	<b>18</b>	<b>59</b>	<b>75</b>

Balance Sheet (A\$m)	FY19A	FY20E	FY21E	FY22E	FY23E
Cash	5	54	18	59	75
Other Current Assets	0	0	0	0	0
PP&E	2	44	172	145	124
Exploration & Development	34	38	41	45	49
Other Non Current Assets	-	-	-	-	-
<b>Total Assets</b>	<b>41</b>	<b>137</b>	<b>232</b>	<b>250</b>	<b>249</b>
<b>Debt</b>	<b>-</b>	<b>-</b>	<b>100</b>	<b>50</b>	<b>-</b>
Other Liabilities	15	15	15	29	30
<b>Net Assets</b>	<b>26</b>	<b>122</b>	<b>117</b>	<b>171</b>	<b>219</b>

Ratio Analysis		FY19A	FY20E	FY21E	FY22E	FY23E
Diluted Shares	m	286	954	954	954	954
EPS - Diluted	Ac	(1.0)	(1.2)	(0.5)	6.6	7.0
<b>P/E</b>	<b>x</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>1.7x</b>	<b>1.6x</b>
CFPS - Diluted	Ac	(0.3)	(1.0)	(0.4)	11.1	9.6
<b>P/CF</b>	<b>x</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>1.0x</b>	<b>1.1x</b>
FCF - Diluted	Ac	(0.7)	(4.9)	(13.8)	11.8	9.6
<b>P/FCF</b>	<b>x</b>	<b>n.m.</b>	<b>n.m.</b>	<b>n.m.</b>	<b>0.9x</b>	<b>1.1x</b>
Dividends	Ac	-	-	-	2.0	2.0
Dividend yield	%	-	-	-	18.2%	18.2%
Payout Ratio	%	-	-	-	30%	28%
Franking	%	-	-	-	100%	100%
Enterprise Value	A\$m	27	(23)	113	22	(44)
<b>EV/EBITDA</b>	<b>x</b>	<b>n.m.</b>	<b>5.1x</b>	<b>n.m.</b>	<b>0.2x</b>	<b>(0.4x)</b>
ROE	%	(10%)	(4%)	(4%)	37%	31%
ROA	%	(7%)	(3%)	(2%)	25%	27%
Net Debt / (Cash)		(5)	(54)	82	(9)	(75)
Gearing (ND/(ND+E))	%	(23%)	(80%)	41%	(6%)	(52%)
Gearing (ND/E)	%	(19%)	(44%)	70%	(5%)	(34%)

Reserves & Resources	Updated: October 2018			
M+I+I Resources	mt	Cu %	Zn %	CuEq %
Sulphur Springs	13.8	1.5%	3.8%	3.0%
Kangaroo Caves	3.6	0.8%	6.0%	3.2%
Whim Creek	1.0	1.4%	1.2%	1.9%
Other	7.6	1.0%	2.0%	1.9%
<b>Total</b>	<b>26.0</b>	<b>1.2%</b>	<b>3.5%</b>	<b>2.7%</b>

P+P Reserves	mt	Cu %	Zn %	CuEq %
Sulphur Springs	8.5	1.4%	3.1%	2.7%

Earnings Sensitivity		FY22E	FY23E	FY22E	FY23E
		A\$m	A\$m	%	%
Copper Price	US\$/lb +10%	15	12	23%	18%
Zinc Price	US\$/lb +10%	2	6	2%	9%
Exchange Rate	A\$/US\$ -10%	16	19	25%	28%

Valuation	Discount	Stake	A\$m	A\$/sh
Sulphur Springs (unrisked)		100%	372	1.30
Sulphur Springs (risk-adjusted)	60%	100%	149	0.52
Exploration & Projects			35	0.12
Corporate & Other			(34)	(0.12)
Debt			-	-
Cash			2	0.01
Option Strikes			-	- P/NAV
<b>Risk adjusted NAV</b>			<b>152</b>	<b>0.53</b>

Source: Company data, Blue Ocean Equities

**MODEL SUMMARY: OPERATIONAL INPUTS & FREE CASH FLOW**

<b>Operational Summary</b>						
		FY19A	FY20E	FY21E	FY22E	FY23E
<b>Sulphur Springs - Mining</b>						
<u>Open Pit</u>						
Open Pit Ore Mined	mt	-	-	-	0.87	1.25
Open Pit Waste Mined	mt	-	-	5.0	10.4	10.1
Strip Ratio (Waste:Ore)	X-1	-	-	-	12.0	8.1
Open Pit Copper Grade	%	-	-	-	3.0%	1.6%
Open Pit Zinc Grade	%	-	-	-	1.6%	3.0%
<b>Open Pit CuEq Grade</b>	<b>%</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>3.7%</b>	<b>2.8%</b>
<u>Underground</u>						
Underground Ore Mined	mt	-	-	-	-	-
Underground Copper Grade	%	-	-	-	-	-
Underground Zinc Grade	%	-	-	-	-	-
<b>Underground CuEq Grade</b>	<b>%</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Sulphur Springs - Processing</b>						
Mill Throughput	mt	-	-	-	0.87	1.25
Copper Head Grade	%	-	-	-	3.3%	1.9%
Copper Recovery	%	-	-	-	83%	85%
<b>Copper-in-conc Produced</b>	<b>kt</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>24</b>	<b>20</b>
Zinc Head Grade	%	-	-	-	0.9%	2.5%
Zinc Recovery	%	-	-	-	88%	88%
<b>Zinc-in-conc Produced</b>	<b>kt</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>7</b>	<b>28</b>
CuEq-in-conc Produced	kt	-	-	-	26	31
<b>Group</b>						
		FY19E	FY20E	FY21E	FY22E	FY23E
<b>Copper-in-conc Produced</b>	<b>kt</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>24</b>	<b>20</b>
C1 Cost (post credits)	A\$/lb Cu	-	-	-	1.48	0.97
Royalties	A\$/lb Cu	-	-	-	0.28	0.38
Sustaining Capex	A\$/lb Cu	-	-	-	0.03	0.07
<b>All-in Sustaining Cost</b>	<b>A\$/lb Cu</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1.79</b>	<b>1.42</b>
All-in Sustaining Cost	US\$/lb Cu	-	-	-	1.22	0.96
<b>Sulphur Springs</b>						
	A\$m	FY19A	FY20E	FY21E	FY22E	FY23E
Copper Revenue		-	-	-	220	183
C1 Cost (post credits)		-	-	-	74	40
Royalties		-	-	-	14	16
Sustaining Capex		-	-	-	1	3
All-in Sustaining Cost		-	-	-	89	59
<b>All-in Sustaining Margin</b>		<b>-</b>	<b>-</b>	<b>-</b>	<b>131</b>	<b>129</b>
Growth Capex		-	43	128	-	-
Exploration		4	4	4	4	4
<b>All-in Margin</b>		<b>(4)</b>	<b>(47)</b>	<b>(132)</b>	<b>127</b>	<b>125</b>
<b>Corporate</b>						
	A\$m	FY19A	FY20E	FY21E	FY22E	FY23E
Cash Tax		-	-	-	13	28
Corporate & Other		1	4	4	5	10
<b>FCF pre Debt Service</b>		<b>(5)</b>	<b>(51)</b>	<b>(136)</b>	<b>109</b>	<b>87</b>
Net Interest		0	-	-	8	2
Debt Drawdown / (Repayment)		2	-	100	(50)	(50)
<b>FCF post Debt Service</b>		<b>(3)</b>	<b>(51)</b>	<b>(36)</b>	<b>50</b>	<b>35</b>
<b>New Equity/Dividends</b>						
	A\$m	FY19A	FY20E	FY21E	FY22E	FY23E
Proceeds from Shares/Options		6	100	-	-	-
Dividends Paid		-	-	-	10	19
<b>Change in Cash</b>		<b>2</b>	<b>49</b>	<b>(36)</b>	<b>41</b>	<b>16</b>
<b>Cash Balance</b>		<b>5</b>	<b>54</b>	<b>18</b>	<b>59</b>	<b>75</b>

Source: Company data, Blue Ocean Equities

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Steuart McIntyre does not own shares in Venturex Resources.