



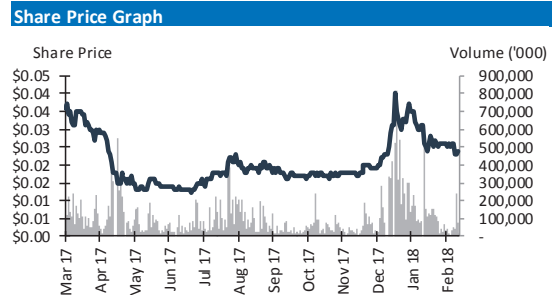
Atlas Iron Limited (AGO)

DSO and royalties forgotten amid deep discounts

Recommendation	Buy			
Previous	Buy			
Risk	High			
Price Target	\$ 0.037			
Previous Target	\$ 0.040			
Share Price (A\$)	\$ 0.024			
ASX Code	AGO			
52 week low - high (A\$)	0.012-0.04			
Capital structure				
Shares on Issue (M)	9,280			
Market Cap (A\$M)	223			
Net Cash/(Debt) (A\$M)	2			
EV (A\$m)	221			
Options on issue (M)	333			
12mth Av Daily Volume ('000)	99,976			
Y/e Jun earning A\$M	2017a	2018e	2019e	2020e
Sales	871.1	618.5	744.0	586.1
EBITDA, adj	135.1	43.4	63.4	70.9
NPAT, adj	48.0	-31.8	-2.1	5.3
EPS, adj c	0.51	-0.34	-0.02	0.06

Board	
Eugene Davis	Non-Executive Chairman
Cliff Lawrenson	Managing Director
Daniel Harris	Non-Executive Director
Alan Carr	Non-Executive Director
Cheryl Edwardes, AM	Non-Executive Director

Major Shareholders	
Legg Mason Inc.	6.8%



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The analyst does not own AGO securities.

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

Cranport Pty Ltd owns 19,000,000 AGO shares.

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Event:

- **1H18a result.**

Analysis:

- **1H18a result highlights:** AGO reported a net loss of \$21.3M in 1H18a, below our estimates (FSBe \$11M), on revenue of \$308M, as lower grade discounts persisted and increased costs arose from haulage, freight, and lower volumes.
- **AGO's shifting product mix to counter discount and help with margin in CY19e:** now targeting 55%:45% lump and fines mix (previously 40% lump), as discounts continue to put pressure on margin. Customer acceptance is growing for lower impurities ore, with expectations for better pricing for this tailored product. The company is also looking to add lithium DSO into the product mix before FY18e end.
- **Lithium DSO from Pilbara Minerals (PLS) on track for April 2018e.** Minimum of 1Mt of 1.5% lithium DSO, and up to 1.5Mt over the next fifteen months to monetise AGO's existing infrastructure for an estimated **\$30M EBITDA contribution**. AGO expects an operating margin of A\$15-20/t lithium DSO. We have assumed 1.5Mt of DSO from April 2018e, and a price of US\$120/t for Li 1.5% DSO.
- **Altura Mining (AJM) royalties to boost cash flow in FY19e:** 5% gross sales royalty to AGO from AJM's Pilgangoora production expected to generate ~\$5M cash per year from FY18e onwards. We estimate ~A\$50M value from the stream. We anticipate a progress announcement shortly.
- **Any additional cash will give AGO options, and likely to allow continued inroads into debt reduction.** Term Loan B was A\$103M at 31 December, while cash was A\$105M, with a \$20M debt repayment made in early January 2018. AJM royalty stream windfall likely to be applied to debt.

Earnings and Valuation:

- We now forecast FY18e and FY19e EBITDA of \$43M and \$63M (previously \$98M and \$93M) and FY18e and FY19e NPAT of -\$32M and -\$2M (previously \$23M and \$18M), due to increased costs and discounts.
- We have decreased our valuation to \$0.037/share (previously \$0.04) based on our DCF valuation, as a result of higher product discount and costs. We believe there is upside from shifting product mix and improvement in discounts.

Recommendation:

- We maintain a **Buy recommendation** on AGO with a decreased **price target of \$0.037 (previously \$0.04)**, in line with our DCF valuation. Revenue diversification through mining services is a welcome addition to the portfolio.
- We see positive catalysts for the stock include 1) further AGO infrastructure utilisation via lithium DSO agreements; 2) updates on royalty monetisation; 3) further debt reduction; 4) development updates on further growth opportunities in iron ore and other commodities.