



TerraCom Ltd (TER.ASX)

Blair Athol delivers and a better half to come

Event:

- Review of interim result; earnings changes.

Investment Highlights:

- TER reported interim NPAT loss of **-\$14.2M**, bettering our forecast of **-\$19.9M**, and EBIT was **-\$0.5M** vs our estimate of **-\$3.3M**. Key differences were lower D&A and tax expense. EBITDA was \$5.5M in-line with our forecast of \$5.4M.
- Australia performed better than we anticipated, yielding EBIT of **\$2.2M** (FSBe **-\$4.4M**) with net EBITDA margin of **US\$11/t** due to lower operating costs than we had estimated. The margin was achieved despite Blair Athol undergoing restart and ramp up during the half and shipping through third party rail load out (RLO).
- We expect 2H to improve as Blair Athol will have a full six months at nameplate plus will have its own RLO commissioned end March. The mine achieved 500kt shipped on March 7th, which implies the 2H to date is tracking in-line to the 1.7Mtpa saleable nameplate production rate (2Mtpa ROM).
- Mongolia fared worse than our estimate, mostly due to higher operating costs. Net EBITDA margin was US\$7/t vs our estimate of US\$20/t. Commissioning of wash plant in mid-CY2018 is critical to improving profitability.
- TER ended the half with **\$1.1M cash (pro-forma \$16.1M post recent equity raise) and debt of \$198.5M**. We forecast TER will be able to service its interest and debt commitments over FY18e-FY20e from cash flows, but may need to raise equity and/or refinance when Euroclear bond matures in FY21e. Working capital ratio was low with increase in payables greater than that of inventory and receivables. We expect payables to gradually wind down and inventories at Blair Athol to reduce in 2H especially as RLO is commissioned.

Earnings and Valuation:

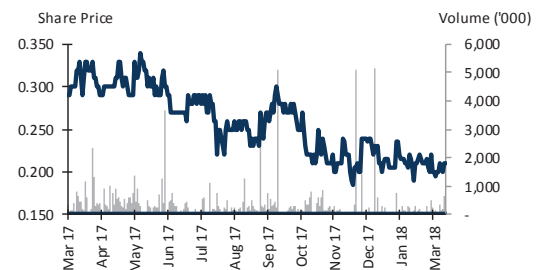
- We have downgraded NPAT for FY18e to a loss of **-\$9M** (prior **-\$4M**) while upgrading FY19e to **\$83M** (from **\$59M**). The downgrade in FY18e is due to higher operating costs at Mongolia, partially offset by lower Corporate and Blair Athol costs. For FY19e, our upgrade is due to lower Blair Athol costs driven chiefly by its own rail load out, partly mitigated by higher Mongolia costs.
- Our risked valuation of TER has reduced to **\$0.65/share** (previous **\$0.69/share**) mostly due to reduction in value of Mongolia assets, partially offset by increase in Blair Athol valuation. The latter has now surpassed our valuation of BNU.

Recommendation:

- We maintain our **Buy** recommendation, and reduce our 12-month price target to **\$0.65/share** (prior **\$0.69**) in line with our revised valuation. We expect improvement in 2H earnings mostly from Blair Athol as it contributes for a full six months and commission its own RLO. However FY19e is a critical year as the commissioning of the CHPP at Mongolia should have a step change impact on BNU's earnings.
- Catalysts for share price include 1) Commissioning of Blair Athol rail load-out facility; 2) Commissioning of BNU CHPP; 3) Higher coal prices; 4) Reduction in net debt; 5) Reserve and Resource upgrades; and 6) Generation of underlying net profit.

Recommendation	Buy			
Previous	Buy			
Risk	High			
Price Target	\$0.65			
Previous	\$0.69			
Share Price (A\$)	\$ 0.220			
ASX Code	TER			
52 week low - high (A\$)	0.15-0.36			
Valuation (A\$/share) - risked	\$0.65			
Methodology	DCF			
Capital structure				
Shares on Issue (M)	372			
Market Cap (A\$M)	82			
Net (Debt)/Cash (A\$M)	-182			
EV (A\$M)	264			
Options (M)	3			
Warrants (M)	13			
Fully diluted EV (\$M)	267			
12mth Av Daily Volume ('000)	352			
Y/e Jun (A\$M)	2017a	2018e	2019e	2020e
Sales	22.5	164.9	350.0	317.5
Underlying EBITDA	-19.2	38.0	142.9	110.9
Underlying NPAT	-56.8	-9.1	83.1	45.4
NPAT reported	5.0	-9.1	83.1	45.4
EPS diluted adj. \$	-0.20	-0.03	0.21	0.12
PER x diluted	nm	nm	1.0	1.9
EV/EBITDA x	nm	8.6	2.3	2.9
Board				
Wal King	Non-Executive Chairman			
Craig Wallace	Non-Executive Deputy Chairman			
Michael Avery	Executive Director			
Matthew Hunter	Non-Executive Director			
Tsogt Togoo	Non-Executive Director			
Phillip Forrest	Non-Executive Director			
James Soorley	Non-Executive Director			
Substantial Shareholders				
OCP Asia	17.6%			
Noble Resources International	9.9%			

Share Price Graph



Analyst: Mark Fichera

+612 9993 8162

mark.fichera@fostock.com.au

The analyst owns 65,000 TER shares.

Foster Stockbroking and associated entities (excluding Cranport Pty Ltd) own 1,295,770 TER shares, 1,500,000 options at exercise price \$0.30 expiring August 2018, and 1,500,000 options exercise price \$0.45 expiring August 2018. Cranport Pty Ltd owns 3,531,324 TER shares.