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Expect to hit paydirt as zircon mines take off

TIM BOREHAM

While resources pundits regard copper as the commodity most reflective of the world's economic strength or otherwise, the more obscure zircon arguably is an even better guide.

On zircon's recent price strength, investors shouldn't be fretting about a global recession or a Chinese downturn.

A component of mineral sands, zircon is used in ceramics and for heavy-duty manufacturing such as nuclear reactor liners and jet turbine blades.

It's also used to make artificial diamonds and is even being talked about as a future battery metal material.

With the depletion of some of the bigger deposits and with few new finds of note, the zircon price is on a tear: up from a recent low of $US950 a tonne in mid 2016 to $US1650 now.

Australia is the biggest zircon producer, accounting for 35 per cent of global output. Consultant TZMI expects zircon demand to grow by 2.8 per cent a year to 2026, from the current 1.2 million tonnes. At the same time, supply is expected to decrease by 4.3 per cent a year.

"It's a good time to be in the zircon business," says Diatreme Resources head Neil McIntyre. "We see constrained supply: mines are maturing so there's a strong window for new projects to meet that shortfall."

The earnings turnaround is already apparent at **Iluka Resources (ILU, $8.64)**, our biggest mineral sands producer, which posted a June-half net profit of $126 million, compared with an $81m loss previously.

But after years of development and promises, three other local minnow developers are poised to become producers at the right time.

Peaking the excitement scale is **Sheffield Resources (SFX, 88c)**, which for a small cap is in the enviable position of fully owning Thunderbird, one of the biggest mineral sands discoveries in the past three decades.

Thunderbird in WA is close to being "go", at least for the $463m first stage: a $US175m ($242m) debt facility has been arranged (although it's non-binding at this stage) and the Northern Australian Infrastructure Fund is chipping in $95m.

Management is negotiating an engineering, procurement and construction contract, which is expected to be fixed price in order to minimise risk.

The company targets production by the December quarter of 2020, with initial output of 122,000 tonnes increasing to a substantial 809,000 tonnes by 2025. A bankable feasible study in March ascribed a net present value to Thunderbird of $US507m, but that was when rutile traded around $US1380 a tonne.

Meanwhile, **Image Resources (IMA, 12.5c)** has announced commissioning of its Boonanarring mineral sands project in the North Perth basin, 80km north of the capital.

The project's proximity to Perth means it will be a cheaper drive-in drive-out than a less hospitable fly-in fly-out one.

"The company has been working diligently over two years to move a company into production," Image chief Patrick Mutz told the Australian Micro-cap Investment Conference.

Indeed, If Image can get its ducks in a row Boonanarring could be producing by as early as Christmas, based on a simple dry shovelling operation.

The company is fully funded, not only to complete construction but has the funds for the working capital through the commissioning to ramp up to positive cash flow.

Rutile is the key ingredient in mineral sands, which in Image's case means a mix of zircon, rutile, leucoxene and ilmenite.

While zircon will comprise 30 per cent of the heavy mineral concentrate produced, it is expected to account for three quarters of the project's revenues.

The project economics look good. Updated in June, the bankable feasibility study values the project at $235m, with a project cost of $52m and a payback period of 13 months.

The project is forecast to produce earnings before interest and tax of $278m over its life, although zircon's further price strength mean these numbers could be conservative.

The company envisages annual output of 220,000 tonnes of heavy mineral sands, containing 60,000-70,000 tonnes a year of zircon.

Overall, Boonanarring is rated as a 19.8mt resource, grading 7.2 per cent heavy minerals. As Mutz proudly notes, that's more than twice the grade of a typical deposit globally.

Sheffield shares have retreated sharply after hitting $1.20 in early October, despite talk that Thunderbird would make for better economies if it were in the hands of a major.

In other words, Sheffield is a takeover target.

In the case of all three stocks, investors should be aware that once a developer starts digging, the shares tend to underperform because the stock is being valued on the drudgery of reality rather than blue sky.

Pundits who believe in the

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mineral sands story could well consider Iluka: rather than revelling in the buoyant prices, the shares have slumped 30 per cent since late August because the company's costs guidance for the 2018 calendar year were higher than expected.

Iluka's $3.65 billion market cap compares with $218m for Sheffield, $123m for Image and $23m for Diatreme.

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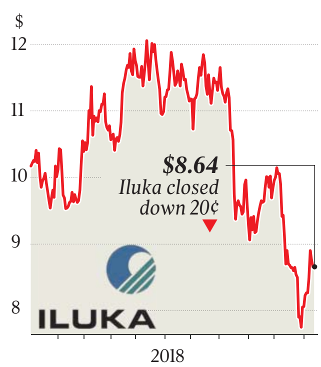

Source: Bloomberg