

Lucapa Diamond Co. Ltd

(LOM \$0.295) Speculative Buy

EUROZ

Analyst	Date	Price Target
Greg Chessell	8 th May 2017	\$0.57/sh

Company Update

Investment case

Lucapa is an emerging play on the high value end of the diamond market, a robust segment due to scarcity of supply and increasing number of wealthy individuals globally. The Lulo alluvial diamond mining operations, producing the highest average diamond value of any mine in the world, is on course to achieve a similar gross sales outcome as in 2016. The imminent end of the Angolan wet season should enable greater productivity in both mining and exploration. Exploration for the kimberlite source is exciting, and if successful should result in a significant re-rating. The size and shape of alluvial diamonds recovered suggest the source is close by. The impending distribution from SML will provide Lucapa much of the capital required to settle the Mothae acquisition. Mothae is an exciting medium term high value Kimerlite diamond development opportunity.

Key points

- Lulo (LOM 40%) production in Mar Q'17 of 4.1kct compares with 5.3kct in Dec Q'16, and 3.1kct in pcp. A sound result in context of this wet season affected period.
- SML, the incorporated JV owner of Lulo, sold two diamond parcels for aggregate US\$10.7m (4,498ct at an average of US\$2,379/ct). This is on-track with our annual forecast of 21kct at US\$2,500/ct, when seasonally adjusted.
- A parcel of 1,919ct was sold subsequent to the Mar Q'17 for US\$2.5m, taking gross sales to US\$13.2m ytd.
- Diamond inventory was 2,545ct at end Mar Q'17 (v's 1,346ct Mar Q'16).
- Mining was confined to the MB28 pit, which contains a thicker sequence of gravel, lying at a higher level, allowing record earthmoving productivity. However grade (5.8 v's 10.5ct/100m³ in 2016) and average stone size (1.2ct/stone v's 1.7ct/stone in 2016) is lower.
- The wet season will draw to a close during the June Q, resulting in production in the first half of the period continuing to be sourced from the MB28 pit. Mining will shift to the higher grade MB 6 & 8 pits once conditions permit, probably late in the period.
- Lucapa holds cash of US\$2.1m and Nil debt at end March'17, prior to receiving distributions (below).
- SML declared an US\$8m distribution during March, comprising 50% loan repayment to Lucapa (US\$4m) and 50% dividend to shareholders (Lucapa's 40% = US\$1.6m). The balance owed by SML to Lucapa is reduced to US\$29m.
- Lucapa intends to retain the dividend in Angola to fund Kimberlite exploration, while the loan repayment is awaiting NBA approval for repatriation.
- SML retains cash of US\$11m at end March, after providing for the US\$8m distribution, and prior to the US\$2.5m sale in early April. We estimate SML generated net cash of -US\$30m in the 12months to March 2017.
- LOM's annual report to Dec'16 revealed SML generated US\$10.4m NPAT for the 7.5 months since incorporation in mid May 2016 (LOM share US\$4.1m). Significantly this was generated on a PBT margin of 51%.
- Lulo alluvial mining JORC Inferred resource update showed 10% higher insitu volume at 14% lower grade, for overall 5% lower contained carats despite 22kct depletion in the 15 month intervening period. The estimated carat value has increased >50% to US\$1,246/ct, but is significantly below the US\$2,300/ct achieved project to date.

Lucapa Diamond Co	Year End 31 Dec	
Share Price	0.295	\$/sh
Issued Capital		
Fully Paid Ord	327	m
Options (m)	\$0.20	46 m
Options (m)	\$0.30	3 m
Options (m)	\$0.53	3 m
Perf Rights		2 m
Total Diluted	379	m
Mkt Cap (dil)	102	\$m
Enterprise Value	99	\$m
Debt	0	\$m
Cash	3	\$m
Turnover	2.0m sh/day	
12 mth Lo-Hi	\$0.21 - \$0.55	
Balance Date	31st Dec	

Directors

M Kennedy	Chair
S Wetherall	CEO
G Gilchrist	NE Dir
A Thamm	NE Dir
N Selby	COO

Shareholders

Carrington	6.1%
Dir & Mgt	1.0%

Company Details

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Share Price Chart



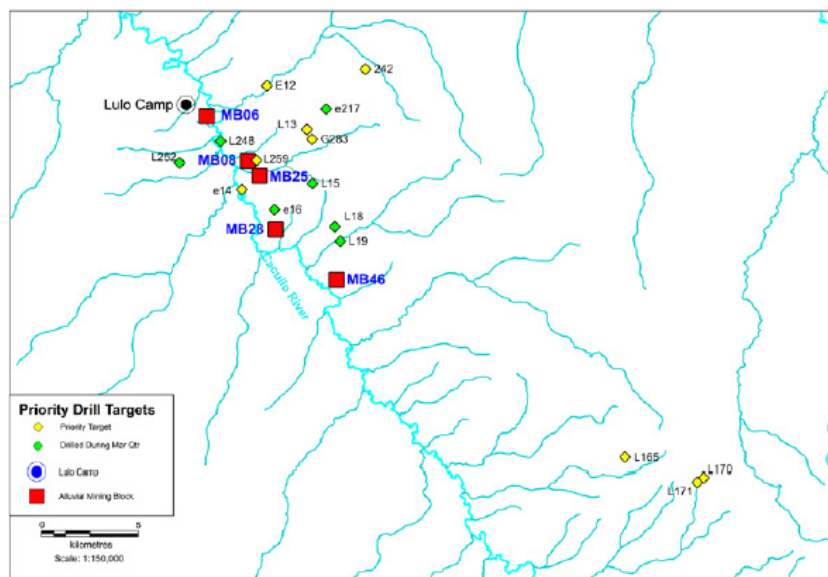
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- The resource volume will sustain >4 yrs of mining at the 20kbcm/mth rate. Lucapa endeavours to maintain a 4 – 5 year inferred mine life based on resources on the Cacuillo River. Exploration for alluvial diamond gravels on the adjacent Lulo River will commence in the June Q following construction of an access road.
- Exploration for the kimberlite source will gather momentum as the dry season approaches, with 3 drill rigs on-site.
- Drilling of target L15, 3.5km from prolific alluvial mining block (MB8), intersected prospective shallow coarse re-sedimented volcanoclastic kimberlite in the 1st hole. A further 5 holes are planned. Drilling of targets L13, E16, L248, E217 are also planned for the current period.



Source: Lucapa Diamond Co. Ltd

- Acquisition of 70% stake in the Mothae kimberlite project, Lesotho, remains on track with confirmation of the JORC resource and grant of a 10 year mining licence. A US\$4.1m payment to Gov't of Lesotho is due in late May 2017. A further US\$4.5m is due in 8 monthly instalments. Lucapa intends to fund the acquisition through the impending distribution from SML, and exercise of share options.
- Mothae hosts a large resource of high value diamonds. JORC Resource estimate is 39mt grading 2.7cpt with an estimated value of US\$1,063/ct. Trial mining of a 600kt parcel yielded 23kct, with several large stones (including 254ct, 82ct, 56ct=US\$1.7m, 53ct, 45ct, 29ct=US\$1.2m, 14ct=US\$0.4m).
- Lucapa intends to commence mining at Mothae at a rate of 0.7mtpa from the near surface oxidised material, recovering some 22kctpa, generating gross sales of -US\$26mpa, after an investment of US\$12m which will be repayed within 18 months. A larger scale development is contemplated subsequently.
- The market for large rough diamonds is understood to remain strong, supported by investment by the ever increasing volume of uber-wealthy individuals. Lucara Diamonds (LUC.TSX) sales of large stones from Karowe show a divergence of price performance between the large stone market which remained firm and small stone market which weakened in 2015/16, in part due to the demonetisation program in India and competition from synthetic diamonds. Indeed AngloAmerican has recently reported stabilisation in the small stone market citing "improved demand for lower value goods in stock at 31 Dec 2016".

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Valuation	A\$m	A\$/sh
SML (LOM sh)	97	0.25
Kimberlite (LOM sh)	51	0.14
Mothae (LOM sh)	40	0.10
Other Expl'n	7	0.02
LOM Cash	3	0.01
LOM Debt	0	0.00
LOM WC	7	0.02
Unpaid Capital	11	0.03
Total	215	0.57

Lucapa Diamond Co - Euroz Cashflow and Operating Estimates															
	Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec	2016	Mar	Jun	2017	Project	F'cast	
	Q'15	Q'15	Q'15	Q'15	Q'16	Q'16	Q'16	Q'16	act	Q'17	Q'17	2017	Project	F'cast	
SML (Alluvial)	act	act	act	act	act	act	act	act	act	act	act	ytd	to date	pa	
Strip Ratio	8.1	4.3													
Treated	13	17	44	38	37	37	65	50	189	71		71	373	210	
Recovered	1,335	1,430	3,479	2,151	3,088	2,581	8,853	5,313	19,835	4,098		4,098	32,328	21,000	
Grade	10.3	8.3	7.9	5.6	8.3	7.0	13.7	10.6	10.5	5.8		5.8	8.7	10	
Stones	1,317	1,818	2,896	1,594	2,260	2,051	4,561	2,838	11,710	3,544		3,544	22,879		
Carats/Stone	1.0	0.8	1.2	1.3	1.4	1.3	1.9	1.9	1.7	1.2		1.2	1.4		
Specials	12	3	43	28	23	30	137	79	269	38		38	393		
Specials	195	96	1,030	764	1,285	683	3,210	1,898	7,076	1,129		1,129	10,290		
Specials %	15%	7%	30%	36%	42%	26%	36%	36%	36%	28%		28%	32%		
Special Size Avg		32	24	27	56	23	23	24	26	30		30	26		
Sales		2,989	2,559	3,778	1,931	2,670	7,837	4,676	17,114	4,498		4,498	30,938	21,000	
Sales	US\$m	2.9	0.7	5.8	23.1	3.0	10.3	14.6	51.1	10.7		11	71	52.5	
Price Rec'd	US\$/ct	976	280	1,538	11,983	1,132	1,319	3,122	2,986	2,379		2,379	2,303	2,500	
Sales	A\$m	3.7	1.0	8.1	32.5	4.1	13.6	19.5	69.8	14.2					
Price	A\$/ct	1,227	400	2,141	16,831	1,546	1,741	4,169	4,076	3,151					
FX	A\$1=US\$	0.795	0.702	0.718	0.712	0.731	0.758	0.749	0.732	0.755				0.76	
Inventory	ct				1,779	1,219	2,286	2,921		2,545		2,545			
SML Cash	US\$m					2.0	6.7	14.1		11.1		11.1			
Net Revenue	US\$m	3	1	5	21	3	9	13	46	10		10	64	47	
Opex	US\$m	3	3	3	3	3	4	4	14	4		4	27	16	
Surplus/Deficit	US\$m	-0.4	-2.4	2.2	17.8	-0.3	5.4	9.2	32	5.7		5.7	37	32	
Opex/bcm	US\$/bcm	173	68	78	81	82	60	77	73	55		55	72	74	
Net Revenue/bcm	US\$/bcm	152	15	136	560	74	144	261	243	136		136	172	225	



Source: Lucapa Diamond Co. Ltd

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