

Quick Comment

Lucapa Diamond Co Ltd (LOM \$0.165) Speculative Buy

Analyst	Date	Price Target
Michael Emery	15 th July 2019	\$0.61/sh

June'19 Quarterly

Key Points

- LOM has delivered on key operational goals this Q at both of its high-value diamond mines, Lulo and Mothae, putting it on track to generate op. profit in CY19;
- At the Mothae(70% LOM) kimberlite diamond mine in Lesotho:
 - Diamond cts recovered of 6.3kcts vs 4.6kcts Euroz (up 37%);
 - Grades recovered of 2.39cpht vs 2.0cpht Euroz (up 20%);
 - Recovery of largest gem-quality diamond of 126cts;
 - Cash opex US\$12.56/t (14% lower than plan);
 - Sale of 7,008cts for US\$3.5m during Q at US\$500/ct, with price rec'd likely to increase once mining commences in the higher-margin southern pit from next Q;
 - Unaudited EBITDA of US\$1.1m for June H'19;
- Importantly, these impressive results are from only the second full Q of ops since Mothae reached commercial production and from mining in lower-margin sections of the mine;
- Mining on track to transition to higher-margin diamond zones in Q3 CY19 as higher-margin southern pit is dewatered in conjunction with the construction and filling of the main water dam, Dam 4;



Figures 1 and 2: Water stored in the southern pit (above) being pumped to the new Dam 4 (below) which will enable access to higher-margin diamond zones in Q3 2019

- Mothae had closing diamond inventory of 3,855cts, including the 126ct diamond, with two parcels expected to be sold next Q;

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- At the Lulo (LOM 40%) alluvial diamond mine in Angola:
 - Recoveries of 3.9kcts vs 5.0kcts Euroz (down 23%) as a result of lower throughput (69kbcm vs 75kbcm Euroz) and lower grades recovered (5.6cphm³ vs 7.0cphm³ Euroz);
 - Mining was focussed on areas which produce lower grades and volumes but higher diamond values, as reflected in the sales values for Lulo diamonds and the recovery of a gem-quality 130ct stone during the Q;
 - As dry season commenced, mining is expected to move back into the flood plain blocks from this Q which has historically recovered grades more than twice those of current blocks;
 - Sales for the Q of 5,573cts produced revenues to SML (LOM 40%) of US\$10m at price of US\$1,800/ct, in line with our estimates;
 - H1 CY19 sales of 6,024cts generated revenues of US\$22.1m at an impressive US\$3,668/ct vs Euroz price of US\$1,800/ct and delivered unaudited EBITDA of US\$11.3m for the Half;
 - Value-adding strategy launched with SML partnering downstream to cut and polish select high-value diamonds to maximise future revenues. We expect further details this Q;
- Lulo expansion is underway with new fleet of six excavators and eight trucks arriving to increase production 50% to 450kbcm/year as part of the US\$12m SML-funded expansion. This expansion will increase CF to SML and accelerate loan repayments due to LOM;



Figure 4: New earthmoving fleet arriving on site at Lulo

- Lulo kimberlite exploration program has commenced next phase following extensive technical review of results to-date and includes:
 - Stream sampling of 5kbcm from six major tributaries feeding from high-interest areas where largest diamonds have been recovered;
 - Follow-up delineation drilling of 16 Lulo kimberlite pipes rated most prospective to host diamonds;
 - Drilling eight additional kimberlite targets highlighted in technical review;
 - Program scheduled to take 12 months at cost of US\$3.3m, funded by SML alluvial mining revenues;
 - This is an exciting program for LOM and we believe a discovery here will rapidly rerate the stock to our PT;

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- At Q end LOM had cash of US\$5.2m (down from US\$7.1m Mar'Q) with SML (40% LOM) cash of US\$9m;
- Mothae had diamond inventory of 3,855cts and Lulo 3,147cts;
- We continue to believe the market does not appreciate the bifurcated nature of diamond pricing, with prices of high-value diamonds such as those produced by LOM remaining robust, while low-value diamonds produced by LOM's peers experiencing significant pricing weakness;
- Our Speculative Buy and PT of \$0.61/sh is maintained;

Investment Thesis

Mothae continues to achieve impressive results from lower-margin zones, with mining in higher-margin southern pit due H2 of CY19. We therefore expect positive operating cashflow to be achieved by LOM in H2 CY19. Lulo's 50% expansion of alluvial diamond mining operations has commenced, at a time when the high-value production from Lulo continues to command premium pricing in contrast to lower-quality stones. Expansion to 450kbcm per annum will increase cash generation and is designed to accelerate repayment of -US\$30m loan to LOM from SML. Exploration for the source of Lulo diamonds continues and we expect a discovery will rapidly rerate the stock above our PT.

Lucapa Diamond Co Ltd (LOM)

Share Price	0.165	A\$/sh	Enterprise Value	98	A\$/m
Price Target	0.61	A\$/sh	Debt	22	A\$/m
Valuation	0.61	A\$/sh	Cash	7	A\$/m
Shares on issue	504	m(dil)	Largest ShareholderTazga Two	8.7%	
Market Capitalisation	83	A\$m			

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