18 December 2017

Prairie Mining

Tier 1 assets + perfect macro

Buy

Target price: 90p

Current Share Price:	30.0p
Market Capitalisation:	£50m
Shares In Issue:	167m
EPIC:	PDZ.L
Avg. Daily Volume:	94k
Market:	ASX, AIM
12 Month Hi/Lo:	46p/20p
ISIN:	AU000000PDZ2
SEDOL:	BYSQ580

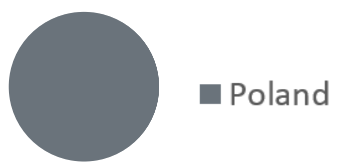
Overview

Prairie Mining is a coking coal project developer focused on two Tier 1 projects in Poland

Share Price History (12m)

Source: Bloomberg

Geographical focus



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Prairie Mining recently published an update describing the coking coal macro in Europe and Poland. The release focused on the European Commission's 2017 critical materials list, the global lack of new coking coal projects, and the Polish government's support for new modern coal mines. We also note how the new Polish Prime Minister is pushing the Polish-Chinese business agenda, which will benefit Prairie Mining.

<u>New Polish Prime Minister</u>

Mateusz Morawiecki recently became Prime Minister and he strongly supports Chinese investment into Poland. Amongst other things, he has recently said "*to encourage Chinese companies to invest more capital in our country*" and "*Poland wants to actively participate in the One Belt, One Road project*".

This agenda fits perfectly with Prairie's strategy of having China Coal construct Jan Karski using <u>low-cost</u> Chinese debt. And we believe support from the new Polish Prime Minister will ensure Jan Karski reaches the point of being fully permitted and funded. As with all major industrial projects, top level government support is essential.

Prairie Mining shares have underperformed our expectations in 2H17 (the shares increased 50% in 1H17). The lack of buying could be due to negative general media surrounding coal. However, Prairie is a coking coal <u>not</u> thermal coal company and has strong political and European macro support . We anticipate 2018 being a good year for Prairie shares and reiterate our BUY recommendation.

Coking coal not thermal—important distinction

Both Prairie's projects are lowest cost quartile coking coal projects. The global drive towards cleaner energy should have no impact on Prairie. Indeed, anything that requires steel including environmentally friendly equipment (electric vehicles, wind turbines, railroads, construction) requires coking coal in the steel production process.

Europe's critical raw materials list — coking coal listed

The European Commission has published 3 Critical Raw Material Lists (2011, 2014 and 2017). The recently published 2017 list includes coking coal. The European steel industry relies heavily on coking coal imports, primarily from the US and Australia.

Coking coal supply outlook—tonnage falling

Over the last 5-10 years there has been limited investment in new coking coal mines. Now consensus is anticipating falling coking coal production over the next 5 years (-5% YoY). This should ensure firm coking coal prices, with the worst case scenario some very short term weakness if there's a global economic slowdown.

Catalysts and recommendation

We anticipate a China Coal feasibility study on Jan Karski to be published in 1Q18. We expect this announcement to include or be shortly followed by a low cost (sub 6%) Chinese debt package covering 70% - 75% of the funding. We regard this as a massive near term catalyst and believe now is a good time to buy the shares. We reiterate our BUY recommendation.

Europe's reliance on coking coal imports

The European Commission has kept coking coal on its 2017 critical list due to Europe's dependence on imports. The critical list has some questionable members, but given the importance of steel and steel's dependence on coking coal, for us coking coal is not one of them.

The fundamentals are clearly very positive, mainly because Europe imports between 63% and 85% of its coking coal requirements* (predominantly from the US and Australia). These imports come with very significant transport costs and mean that European coking coal prices will remain above benchmark prices at US and Australian ports.

In addition, global supply of coking coal is expected to reduce YoY for the foreseeable due to underinvestment over the last 10 years. This is not unique to coking coal but should support prices going forward. Note that current coking coal prices remain strong e.g. Australian coking coal is currently approx. US$200/t versus Jan Karski's and Debiensko's estimated cash costs of $25/t and $47/t respectively.

** depending on source*

Poland's Prime Minister — attracting Chinese investment

On 7th December, Mateusz Morawiecki was named the new Polish Prime Minister. He was previously Minister of Finance and a former CEO of Polish bank Bank Zachodni WBK(part of Santander Group). He is known to be a strong promoter of Chinese investment into Poland. This should assist Prairie and its plan to develop Jan Karski alongside China Coal, and mostly funded through a long term Chinese loan.

Mr Morawiecki quotes include:

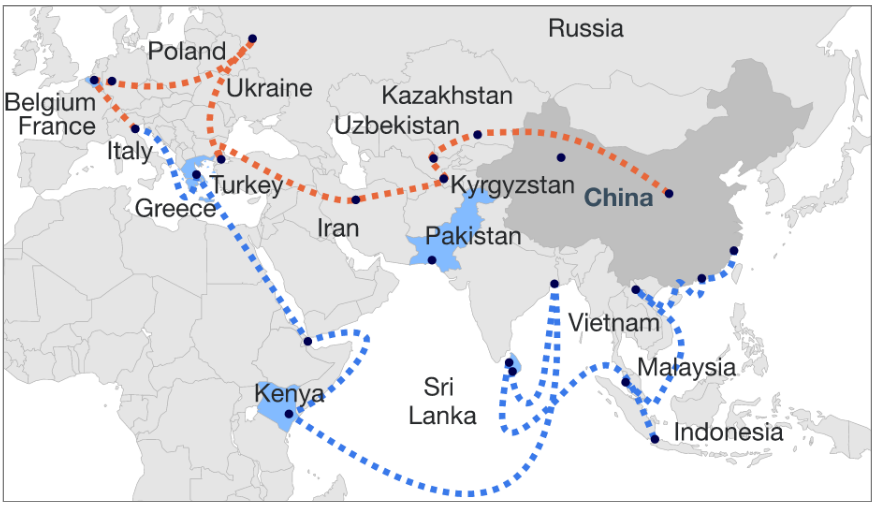
"to enhance Chinese companies to invest more capital in our country"

"cooperation between our countries has great development potential. I am convinced that Poland may become an attractive business partner for China"

"We want to partake in many investments on the One Belt, One Road path, in this great Chinese initiative. We look very positively at it, we are aligned with it"

"I invite our Chinese partners. We already enabled the first few acquisitions of Polish companies by Chinese companies. We are one of the most open countries towards Chinese investors in Europe. We would like to widen this cooperation."

One Belt One Road — Poland the doorway to Europe:



Summary

Europe imports most of its coking coal requirements and is concerned by this reliance. With two Tier 1 coking coal projects in Poland, Prairie is perfectly placed to alleviate this dependence.

We anticipate Prairie securing debt funding for its most advance project (Jan Karski) in 1Q18. Poland's support for Chinese investment adds to the likelihood of this being delivered.

Strengths & Weaknesses

Strengths	Weaknesses
• **Tier 1 projects** – both Prairie's projects are Tier 1 in our opinion. They are lowest cost quartile and are mid to large scale with long mine lives. • **Coking coal macro** – the supply demand fundamentals of coking coal are very positive both globally and in Europe. • **Low cost** – (as above) both Prairie's projects should be low cost, high margin producers. This provides resilience if coking coal prices soften. • **China Coal funding** – although not in place yet, we expect Chinese debt funding to be secured. For Jan Karski in 1Q18. • **Management** – well over 100 years combined coal mine development and operational experience within the company.	• **Funding risk** - We believe that the high quality of both Prairie's projects will result in them being financed with attractive structures for Prairie Mining shareholders. For example, China Coal's involvement at Jan Karski should result in up to 75% of competitive Chinese sourced debt. • **Commodity price risk** – fluctuations in the coking coal price could have an impact on the share price and when in production on revenues and profit margins. • **Licensing risk** – Prairie has the "Exclusive Right to apply for, and consequently be granted, a Mining Concession for Jan Karski". Debiensko is already fully permitted. However, mine permitting is typically a complicated and ongoing process (even once the mine is in production) so should be regarded as a potential area of risk.

Recommendation Breakdown

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