

Standard Lithium Arranges C\$5M Convertible Loan Financing



Figure 1. Building demonstration plant at Lanxess Project site

By the Critical Investor:

It seems more and more likely that Standard Lithium (TSXV: SLL) (OTCQX: STLHF) (FRA: S5L) is displaying a serious commitment of giant JV partner Lanxess these days, with construction of the demonstration plant advancing rapidly along the way. Standard managed to [arrange](#) a C\$5M (US\$3.75M) convertible loan and guarantee agreement with Lanxess on October 30, 2019, and has already been paid out to Standard. The proceedings will be used for the ongoing development of the mentioned demonstration plant, which is capital intensive.

All presented tables are my own material, unless stated otherwise.

All pictures are company material, unless stated otherwise.

All currencies are in US Dollars, unless stated otherwise

According to the [news release](#), the terms are as follows:

“The principal amount of the Loan will be convertible at the option of the Lender at a rate such that for each C\$0.80 of principal converted, the Lender will receive one common share of Standard Lithium (each, a “Common Share”) and one-half of a warrant to purchase an additional Common Share with an exercise price of C\$1.20 per Common Share and a term of three years (each whole warrant, a “Warrant”). Assuming full conversion of the Loan principal, the Lender would receive 6,251,250

Common Shares and 3,125,625 Warrants. All securities issued upon conversion of the Loan will be subject to four-month-and-one-day statutory hold period from the date the Loan was advanced.”

A conversion price of C\$0.80 is reasonable, as the share price at the moment of publication was C\$0.68:



Figure 2. Share price; 1 year time frame

Investors reacted immediately to the positive news, and after a few days of trading at increased volume the stock finds itself at C\$0.75 now (November 5, 2019). If Lanxess would convert into shares, the dilution would be 7% which is very decent. But as it is a loan, the prospect of future dilution is just an option of course for Lanxess. The news release continues:

“The outstanding principal amount of the Loan will bear interest at an annual rate of 3.0%, subject to adjustments. In the event that Standard Lithium has a positive consolidated operating cash flow, as shown on its financial statements, Standard Lithium will pay a fee to the Lender of 4.5% per annum on the average daily outstanding principal amount of the Loan from the issuance date to the date that the consolidated operating cash flow of Standard Lithium is positive. From and after the date on which the consolidated operating cash flow of Standard Lithium is positive, the annual interest rate increases to 7.5%. Pre-payments are permitted with prior written approval of the Lender and are subject to a prepayment fee of 3.0% on the portion of the Loan being prepaid.”

The initial interest rate of 3% is extremely low, meaning C\$150k of annual interest payments until positive consolidated operating cash flow is achieved. The 7.5% rate in production stages is still very fair, as loans fetch often percentages around 10-15% pre-production, as risks are high. Loan periods are often limited (1-2 years) as well, and this is something where Lanxess came in with a more realistic scenario:

“The Loan is due and payable in full on the fifth anniversary, subject to the provision that at any time after second anniversary, the Lender may elect an earlier maturity

date on 60 days' notice to Standard Lithium. The Loan is secured by a charge on the shares of Standard Lithium's direct and indirect subsidiaries (collectively, the "Subsidiaries") Arkansas Lithium Corp. (which operates the Demonstration Plant), Vernal Minerals Corp. (a holding company which owns the shares of Arkansas Lithium Corp.), and 2661881 Ontario Limited (which owns intellectual property rights to be used in the operation of the Demonstration Plant), as well as by a security interest in the tangible and intangible property of Standard Lithium and the Subsidiaries."

A five-year period is very generous for these kind of loans, and to me it speaks volumes about the positive intentions of Lanxess as a JV partner. They really want this to proceed, and if possible make a decent amount of money on equity if successful in my view. This didn't come for free of course, Lanxess wanting to secure the loan against not only the demonstration plant but also the intellectual property rights, as the plant in itself probably only represents an average breakup value of 20-25% at most as it is very specific, which alone would barely cover the principal.

With this money, Standard will be able to complete the construction, installation and first testing of the demonstration plant, which is planned to start commissioning during November. This is one month later than planned in August of this year, but compared to your average pilot plant project this is still very acceptable and hardly worth mentioning. Keep in mind that Standard is planning to raise another C\$10-15M to continue testing and optimizing for the next 12-18 months, which is planned to go on parallel to construction of the large commercial plant if everything works out as hoped, even if Lanxess eventually decided to do so in Q3, 2020. As a reminder, the demonstration plant is designed to continuously process an input tailbrine flow of 50 gallons per minute (gpm; or 11.4 m³/hr) from the Lanxess South Plant, which is equivalent to an annual production of between 100-150 tonnes per annum lithium carbonate equivalent (LCE) (see news release Oct 15,2019)

The demonstration plant is roughly designed at 1/100 of the final nameplate production capacity, should provide sufficient testing data in Q1 2020 for a planned upcoming Pre-Feasibility Study (PFS) in Q2 2020, and if the testing is successful it should be straight forward to scale to nameplate capacity after the investment decision would have been made by Lanxess. The demonstration plant is based on Standard Lithium's proprietary LiSTR technology, that uses a solid sorbent material to selectively extract lithium from Lanxess' tailbrine. The environmentally friendly process eliminates the use of evaporation ponds, reduces processing time from months to hours and greatly increases the effective recovery of lithium.

To see Lanxess seriously providing funding for the first time with hard cash, besides providing Standard with a location for the demonstration plant and the opportunity to test the proprietary lithium extraction process, is noteworthy in my view. Up until this point it was risk-free sailing for Lanxess, having Standard raising all the cash and developing methods, economic studies and demonstration plants. After this loan, things seem to get more serious for the giant chemical company from Germany, as it is very involved in material innovations for batteries and electromobility. Lanxess already offers many

products and solutions along the value chain of lithium-ion batteries, and a wide range of polyamides and polyesters for the electric powertrain. It specifically mentions the project for extraction of lithium from in-house sources besides the other two I just mentioned, indicating the importance for them.

As a reminder: the economics indicate a pretty robust project, at a capex of US\$437M an operation can be constructed with an after-tax NPV8 of US\$989M and an after-tax IRR of 36%, based on an average long term LCE price of US\$13,550/t. I viewed this base case price as high, as it was based on a 3 year average, which is not very realistic in the lithium product realm. However, based on current LCE spot prices of about average US\$11,500/t, after tax figures would still come in economic, and this is important. Depending on successful testing of course. Three scenarios are presented, the 20.9kt LCE pa (per annum) base case, and the hypothetical 30kt LCE pa expansion scenarios:

Standard Lithium PEA Sensitivity						
	20.9kt scenario			30kt scenario		
	25y			25y		37y
LCE pricing	NPV8	IRR		NPV8	IRR	NPV8
\$/t LCE	\$ M	%		\$ M	%	\$ M
10840	564	24,5		774	26,7	722
11743	706	28,3		958	30,5	904
12646	848	32,2		1146	34,4	1085
13550	989	36,0		1331	38,2	1267
14453	1130	39,8		1517	42,1	1448
15356	1271	43,6		1703	45,9	1630
16260	1415	47,5		1889	49,9	1811

Figure 3.

These figures are based on 100% project ownership economics, and 100% equity financed which is standard for economic studies or hypothetical estimates like this. In the news release dated November 12, 2018 Lanxess is committed to provide project finance to the JV when testing and the PFS are successful for them, and Standard will probably be an estimated 30% JV partner (according to company documents filed on Sedar). Regarding the NPV8, I have been very conservative, taking into account that management indicated to me that they expect a lot from optimization programs for brine and processing. This could actually imply improved economics for the upcoming PFS.

As initial capex is US\$437M, and Lanxess would provide financing for the entire project for construction, and as reported in the company's prospectus filed last spring Lanxess will take 100% of the off-take ,the current market cap of Standard Lithium is just C\$69.6M (or US\$52.9M), it seems to make more and more sense to me that Lanxess will buy out Standard outright when testing and PFS proves to be successful, as the Standard market cap is just about 25% of their attributable base case NPV8. Even at a double from now it seems Standard will be a bargain, not accounting for any expansion and/or optimization

programs. I'm very much looking forward to the all-deciding testing that is about to start.

Conclusion

Standard Lithium received another strong vote of confidence from JV partner Lanxess, by providing hard cash. This is a pretty encouraging sign in my view, as up to now Lanxess only provided support through means that hardly cost them anything. As Lanxess is now showing its attention to the importance of electrification with their [New Mobility](#) business (p.54), it seems very interested in production of lithium products themselves, and combined with upside potential for their JV project with Standard and low valuation of Standard compared to NPV8 it doesn't seem very unrealistic for Lanxess to buy out Standard outright when testing and PFS deliver economic results during Q1/Q2 of next year, as the project is already totally in their own backyard, and a potential cash cow bolt-on on existing operations.

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Figure 4.