Sharyn Gol expands operations into value-added products

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Sharyn Gol (SHG:MO) is aggressively jumping into cleaner and more value-added products business to maximize potential revenue streams in coming years.

The Company announced yesterday that it has closed the previously announced tender offer for Naco Fuel (NKT:MO), with the acquisition of 11,723,989 shares, representing 92.9% of Naco. Transaction enables Sharyn Gol to expand its business into highly attractive market for coal briquettes and to increase competitiveness in the Mongolian coal industry. Naco owns a coal enrichment and briquetting plant located in Darkhan, Mongolia. Sharyn Gol intends to return Naco's plant to operation in October 2013.

The air quality problems in Ulaanbaatar have raised the profile of the need for improved (smokeless) coal, and there is potential of at least 500 thousand tonnes of such fuel market, with additional markets in the industrial cities of Darkhan and Erdenet, plus other industrial users. According to National Statistical Office of Mongolia, 11 of 21 provinces of Mongolia do not meet air pollution standards. Naco's plant is ideally situated to enrich Sharyn Gol's coal into clean burning char and smokeless briquettes.

In 2011, the World Health Organization ranked Mongolia's capital Ulaanbaatar (UB) the world's second most polluted city. Ger districts, who rely on coal-fired stoves for heating and cooking, are responsible for 90 percent of winter emissions in the city, according to the World Bank. The Mongolian government has intensified its efforts in improving air quality in UB since 2011, working together with international organizations and foreign donors.

Sharyn Gol is also bringing a wash plant for further expansion into value-added coal products. The purchase agreement of wash plant has already made and the Company started receiving shipments of the plant. The Company expects to complete the feasibility study soon and start pre-commercial trials in November 2013, with full commercialization planned for in the first quarter of 2014.

There are dozens of industrial companies in Darkhan and Erdenet cities such as Erdenet Copper Mine, Darkhan Metallurgical Plant, Erel Cement who use coal products to create their products. Erdenet is the third largest city of Mongolia after “industrial city” Darkhan.

Coal washability test work, performed by Stewart Laboratory, indicated that a product with 6500 kcal/kg heat value, less than 10% ash and 0.5% sulphur (all air dried basis) can be produced with high plant yields. That means it can be improved to become equal with the Newcastle Benchmark, Australian thermal coal being exported to Asia.

Sharyn Gol’s revenue doubled to MNT 9.3 bn in the first 6 months of the year from MNT 4.7 bn a year earlier. Gross profit increased 8 times to MNT 3.1 bn over the same period, whereas gross margin improved to 34% from 8%.

However, the Company reported net loss of MNT 1.4 bn for the six months ended June 30. We expect the Company to post positive earnings, because what matters for Mongolian thermal coal miners is that they post weaker number in the first half of the year than the second half due to more overburden removal and less coal sales occur during the warm weather.

According to management, the Company may lower its production target for the year to around 800,000 tonnes from 900,000 tonnes. The reason is that some power plants that purchase Sharyn Gol’s coal stopped making payments due to their financial problems and some customers had to do unplanned and unscheduled maintenance work, interrupting sales.

Sharyn Gol has mined and sold over half million tonnes of coal year to date, surpassing last year’s sales of 477.6 thousand tonnes.

Sharyn Gol is a leading producer of high-grade thermal coal located in the northern Mongolia. It is a single asset company, owning 100% of the established Sharyn Gol coal mine. A JORC report indicates 374 million tonnes of resource. The Company has been mining coal at Sharyn Gol for over 48 years, supplying domestic customers predominantly for power generation, but also for specialized uses, such as semi-coking end users. 65km long dedicated rail spur, which was built specifically to serve the mining operation, provides direct access to the Trans-Mongolian rail that connects China and Russia.

Abstract Income Statement, MNT `000

	2011 Q2	2012Q2	2012 Q4	2013 Q2
Amount of sales revenue	5,221,992	4,651,451	13,784,353	9,320,288
Cost of goods sold	4,217,872	4,273,852	8,448,041	6,182,327
Gross profit (loss)	1,004,120	377,599	5,336,313	3,137,960
Gross margin	19%	8%	39%	34%
Operational and sub-operational cost	291,559	(1,260,659)	3,220,146	4,380,295
Net profit before tax (loss)	712,561	1,638,258	2,116,167	(1,242,335)

Abstract Balance Sheet, MNT `000

	2011 Q2	2012Q2	2012 Q4	2013 Q2
Cash, cash equivalent	2,798,668	15,951,438	15,018,392	8,395,448
Accounts receivable	1,276,775	1,279,641	3,219,191	3,473,101
Prepaid expenses	175,745	176,620	225,629	1,688,757
Amount of current asset	4,958,599	18,062,028	19,408,194	14,886,171
Amount of non-current asset	15,258,344	16,809,570	21,689,586	29,247,761
Amount of total asset	20,216,944	34,871,599	41,097,780	44,133,932
Account payable	3,068,107	798,811	731,525	3,698,337
Amount of short term liabilities	3,748,606	1,273,365	1,402,611	4,913,150
Amount long term liabilities	2,508,340	-	-	4,081,500
Amount of debt	6,256,946	1,273,365	1,402,611	8,994,651

Source: Company, Mongolian Stock Exchange, BDSec

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