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Light shed on Timminco's high-flying stock

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The incredible upward trajectory in shares of Timminco Ltd. has investors and industry watchers starting to shine a stronger light on the Canadian manufacturer of high grade silicon for the solar industry, which rose out of obscurity over the past two years to become one of the best performers on the Toronto Stock Exchange.

On Friday, shares of Timminco fell 12%, the most in almost three months, to \$22.95, on three times the normal volume. That was after hitting an all-time high of \$28.39 last Wednesday. Still, over the past year, the stock has gained almost eightfold and now has a market capitalization of \$2.4-billion. It's a remarkable achievement, given the company doesn't make a profit.

Timminco certainly has its band of supporters, in large part because of the growing demand for silicon that's used in the solar industry and the company's claims that it can produce very high quality silicon using its patent. Among Timminco's fans is Sprott Asset Management, which owns more than 20% of the company via three entities. That translates into \$500-million, a fair chunk of that profit, given that Sprott Asset Management -- which manages \$6.9-billion in assets and is now in the process of going public -started buying shares at around 40¢.

As well, the company has won kudos from many analysts. Since it doesn't make money, it doesn't have a P/E measure so analysts have turned to a price-to-sales metric, popular in valuing technology companies in the dot.com era.

Clarus recently issued a report, gave the stock a buy rating with a \$40 target. Paradigm Capital liked the story even better: it also gave the stock a buy with a \$43 target. In January, when CIBC World Markets initiated coverage, it termed Timminco "not your average silicon producer" and slapped a \$25 target on the company -or about 24 times the book value of \$1.05 a share (It now has a \$30 target.)

But others are taking a more cautious "show me" stand.

National Bank Financial recently noted that Timminco, which has a new focus on upgraded metallurgical grade silicon, faces new competition. It left its target at \$24.

And Cormark Securities is bearish. In a Jan. 7, 2008, report, it said that "based on its supply agreements, planned capacity and our outlook for weakening poly-Si prices, TIM's stock price is more than fully valued." It has a reduce on the stock with a \$11 target. Since then, Cormark has issued a second report in which it kept the reduce recommendation but raised its target to \$19.50.

The company has also attracted the interest of the short-sellers. At the end of March, according to Bloomberg, 4.616 million shares were shorted, in the United States, up from 831,292 at the end of 2007. On the TSX, a total of 565,040 shares were shorted at the end of March -or more than 300,000 lower than at year end 2007.

Meanwhile, other potential investors continue to do their analysis. One of the country's sharpest, who requested anonymity, has not yet made up his mind. "These guys came out of nowhere, managed to find the holy grail that nobody else could possibly do with no research and development and hardly any capital expenditure. And there's has been no outside corroboration. I think they are heavily overstating the probability of success," he said.

Among the investor's concerns is whether Timminco can achieve its long term purity levels, which means producing silicon that has a very low percentage of phosphorous and boron . As well, the investor asks if can the company generate success once it gets fully operational and is producing 14,400 tonnes per year, up from 300 million tonnes at present. There's also a question of timing, with producers rushing to get supply because of tax incentives in Europe.

Finally, given that the solar grade patent is a key part behind Timminco's success, the investor wonders why there was a six-month gap between the filing of the patent and the announcement. On March 15, 2007, one day after it took a \$33.2-million writedown on its magnesium operations, Timminco announced its first commercial contract for the sale of high purity silicon and said it "has a patent-pending process which enables it to produce high purity (a level of 99.999% purity) or solar grade silicon." The next day, on large volume, the stock jumped 33% to 64 cents.

So what does Timminco say?

Robert Dietrich, chief financial officer, said the company "is a substantial player in silicon," supplying about 3% of the world's market. And the growth in the solar market, the "new" cell manufacturers requires raw material. "An opportunity existed for new entrants into the market and the (four) new entrants are all silicon companies," he said, noting the four that are purifying silicon using metallurgical processes are using different technologies.

The company started developing its technology in 2005 back when a customer made a request to produce very high quality upgraded silicon. In 2006, it did further experimentation off site, set up a pilot plant, and sent samples to prospective customers. "It's not an overnight success story. We used methodology employed in other metals and adapted it to silicon."

As for what this methodology is, Dietrich confirmed speculation that no analyst has seen the production process. "It's a trade secret." he said, noting only the company's employees and its engineering consultants have seen it in action.