Why Did This EV Stock Fall 19% on Wednesday?

Description

Lithium Americas (TSX:LAC)(NYSE:LAC) has been a red-hot electric vehicle theme stock in 2021, until a 19.3% plunge on Wednesday morning. The development stage lithium miner had more than doubled so far this year after a 113% year-to-date gain at close of trade on Tuesday. This was on top of a 284% gain in LAC's stock price in 2020. A rapid and sustained increase in lithium futures prices and wild investor enthusiasm over the huge EV market of the future have driven lithium mining stocks to dizzy valuation heights.

Why did Lithium Americas' stock price fall on Thursday?

The company is raising US$350 million in new equity to fund the development of its Nevada project which recently received the nod from the United States Bureau of Land Management (BLM). After 10 long years of diligent work, the company finally got the authority to go ahead and engage in mining activities at the Thacker Pass lithium project, one of America's largest known lithium deposits.

Lithium Americas announced the pricing of its latest public stock offering on Wednesday morning. The underwritten public offering was priced at US$22 per share, a deep 18% discount to the stock's closing price on the **New York Stock Exchange** the previous day. LAC intends to sell 15,909,091 new shares to the public, and the underwriters have an over-allotment option to buy up to 2,272,727 shares within 30 days after the closing of the deal.

The new equity deal, which is expected to close on Friday, January 22, brings a large supply of new LAC shares into the market. Irrespective of the hefty discount, the new supply should be expected to dampen short-term share price growth.

That said, why would Lithium Americas sell its new shares at a steep discount? Isn't the company leaving a lot of money at the deal table?

Too deep a discount on LAC stock!

It’s no surprise that Lithium Americas’ executives accepted an 18% discount to the stock’s Tuesday closing price. Underwritten public offerings come at a price. Such deals reduce the risk that the company fails to find investors in time. However, bankers want compensation for putting their skin in the game to generate liquidity.

In LAC’s case, bankers had a leeway to negotiate for a deep discount to the deal price for one critical reason:-LAC’s stock had rallied “too much” during the two previous trading sessions.

The company’s announcement of its regulatory breakthrough with the BLM came aftermarket on Friday last week. Shares rallied by 30% between Monday and Tuesday. Such rapid rallies leave volume-weighted average prices way behind. Average prices are usually what deal makers prefer to random closing prices. And the five-day simple moving average on the company’s share price was around US$21.92. This was not far from the US$22 price point, one could say.

Further, deal prices in public offerings are open to heavy negotiation. The final price depends on who has the most bargaining power, at that moment. On one hand, bankers want the deal price to be lower to get the upside advantage. On the other hand, the company doesn’t want to leave too much money on the table. But bargaining power levels aren’t always the same.

For a development stage company that is trying to avoid expensive partnerships and raise project financing directly from the market, bargaining power isn’t always high. Management was bound to accept a discount in this offering. The company was potentially willing to offer incentives to all parties involved.

Time to buy the lithium mining junior?

If you missed the recent rally in Lithium Americas shares, this may offer a second chance to buy-the-dip and profit on lithium’s upside.

Lithium is a critical battery metal. Analysts expect it to be in short supply as industry demand surges by 2025. LAC is one of the most advanced development stage mining stocks in North America and stands to benefit handsomely from a surge in lithium prices.

However, given the latest strong rallies, shares have rallied past fundamental valuation for a development stage lithium mining firm. The company’s Nevada project still has execution risk. Investors that witnessed the collapse of Nemaska Lithium after cost overruns and funding shortfalls in late 2019 will understand the risks involved with project stage companies. I would urge investors to trade with caution.

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