STOCKS DOWN UNDER

1 OCTOBER 2020

Resources Stocks Down Under

> *The best qualification of a prophet is to have a good memory.*

- Lord Halifax (1633-1695) English stateman, writer, and politician

CHALICE GOLD MINES

Who’s this hot girl called Julie Marr?

GENESIS MINERALS

The Odyssey of Ulysses

WALKABOUT RESOURCES

Ready to run

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Stocks Down Under rating: ★★

ASX: CHN
Market cap: A$ 830M

52-week range: A$0.145 / A$2.88
Share price: A$ 2.61

Most of us would rather forget 2020 but not, we suspect, the shareholders of the Perth-based mineral explorer Chalice Gold Mines. On the last day of 2019 the stock was changing hands at 22.5 cents. By 29 September it had gotten to $2.70. If you meet a Chalice shareholder, they're likely to be talking excitedly about a girl named Julie Marr. What they actually mean is Julimar, WA, site of what looks like a massive new nickel discovery not far from Perth. Possibly that excitement has gotten a little excessive in recent days.

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The Odyssey of Ulysses

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ASX: GMD
Market cap: A$ 169M

52-week range: A$0.018 / A$0.089
Share price: A$ 0.088

When investors talk about the Perth-based Genesis Minerals, two projects come to mind – Ulysses in the Eastern Goldfields and Barimaia in the Murchison district. Genesis is in the process of re-establishing the historical Ulysses mine, identifying a resource large enough to support a future standalone development. While Ulysses offers great potential on its own, further expansion along the Ulysses-Orient Well corridor could promote mergers and acquisitions down the line.

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52-week range: A$0.110 / A$0.355
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Walkabout Resources is an energy minerals company with graphite projects in Africa. The company has a high-grade long-life asset in its flagship project in Tanzania, one of the highest margin graphite projects globally. While the mining environment in Tanzania has been less than favourable for explorers in previous years, a recent change in regulations has given Walkabout new confidence in the project's economic potential.

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Share price chart

Source: Tradingview

On Monday 16 March 2020 the world as we knew it was still coming to an end, with the S&P/ASX200 Index down 30% from where it had been just over three weeks previous. However, that was the day it would have been a great time to be a Chalice Gold Mines shareholder. Chalice stock closed at just 16 cents that afternoon. A week later the company announced that its first drill hole at Julimar had brought back some great intersections.

How great? How does 19 metres at 2.6% nickel, 1% copper, 8.4 g/t palladium and 1.1 g/t platinum sound to you? And what if we told you that those 19 metres started at a mere 48 metres below the surface? Wow! Chalice stock, which had been halted since 17 March, returned to trading with a vengeance, closing at 38 cents. It has barely stopped to draw breath since.

Great drill results

Every drill hole that has gone down at Julimar since that fateful March day has reinforced the view that a new future mine just got discovered out in the Western Australian Wheatbelt. Typically, the grades run between 0.5% and a very fat 3.3% nickel, and from 3 g/t all the way up to 15 g/t PGE (platinum group elements). And everywhere Chalice's drill rigs go, the sulphide mineralisation is open in all directions. There's even a decent oxide zone close to surface just to make things really exciting.

Needless to say, a mine this close to Civilisation – on the doorstep of the Avon Valley National Park and about 19 km from a regional town called Toodyay, postcode 6566 – does not lack for infrastructure. The northern Perth suburbs are only about 70 km to the southwest. More importantly, this is not typical nickel country, so no one before Chalice really thought that the ultramafic-mafic intrusions in the neighbourhood counted for anything. That historic neglect has allowed Chalice to get in and stake out in excess of 2,000 sq km in license applications.

If you're bored with Julimar, try Pyramid Hill

And let's not forget the commodities in question, which bode well. Nickel recently made it back above US$15,000 a tonne for a brief time and while platinum at about US$800 an ounce has yet to shake the funk that it has been in since about 2011, the opposite has been true for palladium, now above US$2,000 an ounce thanks to outsize demand from makers of pollution control devices.

The interesting thing about Chalice is that the 2020 re-rating has been all about Julimar and very little about Pyramid Hill, which is a gold project not far from Kirkland Lake's incredible Fosterville mine near Bendigo in central Victoria.

Chalice is sitting on about 5,000 sq km northwest and northeast of Fosterville. A lot of that ground has yet to be drilled by anyone, but the first few holes put down by Chalice have outlined a trend of 4 or 5 km that looks promising. Sure, it's only a metre here or there at a few g/t, but it indicates a gold system worth following up. One suspects the best is yet to come with this project.

The future for this company is still years away

So, what's not to like about Chalice? Well, the thing about the would-be 'company-maker' - Julimar - is that it's still early days, certainly too early for a company with a market capitalisation above $800m. We don't have a JORC resource yet and we probably won't have one until the middle of 2021. What kind of flowsheet will Chalice need for its future mine? Although the kind of rocks that nickel and PGE occur in suggest nothing out of the ordinary will be required, we really don't know yet.

And are there environmental issues with this project? Well, this is the great pro-mining state of Western Australia where everything is generally worked out satisfactorily for all parties, but Chalice's project does partly cover Julimar State Forest, which lets bushwalkers enjoy a nice-looking local Eucalyptus called the 'wandoo'.

What we're saying is that one needs to be careful because Chalice stock is currently discounting a lot of things where the future is somewhat uncertain.

Too much of a good thing?

Chalice is certainly cashed up, with $30m raised at $1.05 a share not long ago. As at June 2020 there was $54m in cash and investments. So, this company will be around for long enough for the questions around Julimar to be answered and maybe to generate a little more excitement at Pyramid Hill.

However, we think the excitement so far has been a little too strong. That's why we are calling it two stars. Since nickel has been cooling off since early September, there is probably risk to the downside, particularly if the folks who got set at $1.05 take some profits off the table. If you have this stock, watch it carefully. That Julie Marr girl may just be too hot to handle right now.

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Share price chart

Source: Tradingview

Genesis' flagship gold project of Ulysses is only 30km from Leonora in the 'Golden Triangle' between St Barbara's Gwalia mine, Saracen's Carosue Dam and Ora Banda Mining's Davyhurst Project. The 867,000-ounce resource covered by Ulysses as at December 2019 sits along the Ulysses-Orient Well corridor (approximately 15km in length), known for its widespread shear-hosted gold system. Genesis has been busy this year acquiring further tenements along the corridor, including the Kookynie Gold Mine from A&C Mining Investments, immediately south-east of Ulysses, for $13.5m. This deal will support the company's strategy of establishing a new standalone gold mine and processing operation. The acquisition, which increased Ulysses' mineral resource estimate to 17 million tonnes at 2.3 g/t gold for 1.28 million ounces, is part of the company's strategy to develop into a mid-tier gold company.

In recent days Genesis has been able to explore further along the highly mineralised corridor that hosts Ulysses. Just east of Kookynie, initial drilling at the Admiral, Clark and Butterfly tenements has yielded an estimated total resource of 4.6 million tonnes at 1.7 g/t gold for 246,000 ounces. The company has also identified significant shallow oxide gold targets at the Archduke prospect, immediately south-east from Admiral-Clark-Butterfly. Genesis will continue with Reverse Circulation drilling at the prospect in the December quarter. That may help the current share price uptrend.

The Kookynie acquisition and promotion related to the associated $19.5m capital raising in June more than doubled Genesis' share price in September to 8 cents from 3.5 cents in January, attracting strong support from shareholders including Alkane Resources (ASX:ALK), which increased its stake from 15.32% to 19.9%.

Transitioning from explorer to mid-tier producer

As is the case for many other junior explorers, the soaring gold price – currently close to US$1,900 per ounce – has allowed Genesis to seize a greater piece of the action. Before Kookynie, Genesis toyed with making Ulysses either a standalone development or a lower-reward toll treatment operation, a practice where smaller companies seek larger producers to process ore. The Kookynie tenements will significantly change the company's independence.

At a price of $13.5m ($33 per ounce), which includes $3m in cash and $10.5m in share payments, Kookynie is also a solid financial investment easily covered by the previous share placement. Kookynie has historically returned high grade gold as recently as the 1990s, so the company will begin infill drilling to confirm the existing resource before completing the Feasibility Study early next year.

Location, location, location

Genesis' fortunes have changed in a relatively short period, with a market cap of only $23m at the end of 2017 and much of that change is down to the company's bullish acquisition and expansion strategy. We believe the company's location and high-grade results set it in good stead for possible expansion and M&A from the bigger producers down the track. The Eastern Goldfields region is an obvious starting point for success: Sons of Gwalia mined Ulysses in 2002 before Genesis took over in 2015 with a smaller resource of 24 million ounces. The company's change from toll operation to an underground mining strategy is due in large part to Genesis' belief in the broader potential of the region's historical open pits.

Sure, Genesis stock has re-rated a lot since the end of the Corona Crash, but we think that has been justified by the company's exploration success as well as the recent transformation of Ulysses. That project might not be pouring gold until 2022, but the outlook for further increases in the resource is high. This stock gets four stars from us.

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Share price chart

Source: Tradingview

Not giving up on graphite any time soon

Aside from Walkabout's flagship Lindi Jumbo Graphite Project in southern Tanzania, the company owns the Eureka Lithium Project in Namibia and holds tenure over the Amani Gold Project in southwest Tanzania. The portfolio is completed by gold and base metal prospects in the UK. However, it's Lindi that is still likely to be the 'company maker' for Walkabout.

Lindi covers a very high-grade deposit of 'Jumbo' graphite where the Total Ore Reserve is 5.51 million tonnes at a healthy 17.9% 'Total Graphitic Content' (TGC). The company's Definitive Feasibility Study in March 2019 outlined a manageable start-up rate of 40,000 tonne per annum of high-grade graphite concentrate and steady production for the next 24 years thereafter. The project has an estimated post-tax Net Present Value of US$197m (A$277m) and an Internal Rate of Return of 119% at a 10% discount. Walkabout has dropped from its December 2019 high of 33 cents, but the company's good fortune in terms of the political situation in Tanzania – which we'll discuss in a moment – has seen a recovery to 24 cents last month.

Lindi Jumbo is so called because it will produce a larger flake size graphite that is in high demand from traditional and specialised non-anode (lithium-ion battery) markets due to its relative shortage. Graphite is a grey crystalline, carbon-based mineral valued for its electrical conductivity and resistance to corrosion. It also varies in concentrate grade and flake size. Size is characterised by four graphite flake types – jumbo, large, medium and fine.

Specific flakes are useful for specific industries with finer flakes in demand for emerging renewables and lithium batteries. Around 75% of Lindi Jumbo's processed graphite is characterised as high purity (TGC 95-97%) according to the latest thinking on flowsheet, allowing Walkabout some confidence in its efforts to attract a high price premium in comparison to similar graphite miners. Natural flake graphite can command anywhere from US$1,300-3,000 per tonne depending on market conditions and product quality.

Opportunity ahead as China looks further afield

The graphite rebound that was supposed to happen in 2020 was knocked by COVID-19, which is probably why Walkabout made the decision to include gold in its portfolio. But there is a generally positive outlook for graphite ahead with a structural supply deficit expected to open up in 2026. And while graphite does have its place as a component in EV technology, that EV boom has taken its time to take off.

Graphite is in demand in non-anode traditional markets (including industrial applications like foundries, refractories and lubricants), enabling Walkabout to continue off-take agreements for Lindi Jumbo's product in those markets. There is a window for Walkabout to sell smaller size graphite flakes as the anode market expands. Given that China is the largest buyer of graphite due to its own limited supply, 2020 has seen more Chinese investment outside of China and this is set to increase further now that the country has committed to a Green Energy target by 2050.

If that wasn't enough, mining regulations in Tanzania are set to ease after a previous tightening. Back in 2017, the country's new Mining Act introduced various measures to ostensibly safeguard the region's natural resources, especially graphite, which had experienced a mini-boom and had attracted numerous foreign companies. Often considered a risky mining region, Tanzania's government has attempted to secure profits from the industry (which makes up more than 50% of the country's exports and is worth around US$960m), but that has often resulted in a chilling effect on foreign investment. While the Act did not significantly change Walkabout's ability to continue its operations (unlike some others), new reforms, including a relaxation in local ownership from 50% down to 20%, should make for a more flexible operating environment, including re-energising foreign investment and capital flow into Tanzania. That's something Walkabout is banking on as it continues to engage with outside parties to fund US$40m (A$53.7m) for Lindi Jumbo.

Walkabout ready to run

Once in production, Lindi Jumbo is forecast to be one of the highest margin graphite projects globally. Walkabout is at a competitive advantage in the initial stage of construction with an updated project capex of only $27.9m. The changes to the Tanzanian mining legislation, while not perfect, do come at a good time for Walkabout as it bases its strategy around graphite and continues to sign binding sales agreements to market its product throughout Asia, Europe and the USA. Walkabout has a cash balance of $2.8m, so it will need to raise money soon. Securing the Amani Gold Project gives the company some flexibility for further growth in a gold region that is largely unexplored and high prospective, but we still think Lindi will attract capital. Walkabout gets four stars from us (and maybe another half star for perseverance).

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Pitt Street Research Pty Ltd is founded on more than 40 years of combined experience researching companies in a range of different sectors.