STOCKS DOWN UNDER

29 OCTOBER 2020

Resources Stocks Down Under

“Africa always brings something new.”

- Pliny the Elder (CE 23 - 79), Roman natural philosopher

AURELIA METALS

Quiet achiever

OKLO RESOURCES

Staying the course in Mali

DEEP YELLOW

A strange case of deja vu

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Quiet achiever

Stocks Down Under rating: ★★★★

ASX: AMI
Market cap: A$ 428M
Dividend yield: 2.04%
52-week range: A$0.21 / A$0.66
Share price: A$ 0.485

Gold-dominant Aurelia Metals currently owns two gold and base metal operations, the Peak and Hera mines, in the Cobar Basin of NSW. Despite some unpredictable production in the last quarter, Aurelia is in it for the long game where its prospects are good. Since the June quarter, Aurelia's share price has dropped from its 66 cent high, but is base-building in the 45-50 cent range.

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52-week range: A$0.115 / A$0.375
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African-focussed gold juniors are making the news these days. Like its neighbour, Chesser Resources (ASX: CHZ), Oklo Resources has been rewarded following exploration success with its gold projects, this time in Mali. The company's share price rose to 37 cents in July following a capital raise to support its gold discovery at Dandoko. Despite some ongoing political complications in Mali, Oklo is worth having on your watch list because the exploration potential is so strong.

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52-week range: A$0.105 / A$0.37
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Deep Yellow is focussed on becoming the next tier 1, low-cost uranium producer with a view to delivering a multi-project portfolio in Namibia and beyond. While Deep Yellow has an experienced uranium background behind it, much seems to depend on the likelihood of uranium making a strong comeback for Deep Yellow's success.

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Share price chart

Source: Tradingview

Steady growth in Q1 FY21

Aurelia's flagship gold projects, the Peak and Hera Gold Mines, can be found in the Cobar Basin in central New South Wales, 550 km west-north-west from Sydney. Though Aurelia is a predominantly a gold company, Peak and Hera are polymetallic in nature, providing the company with access to a range of base metals including silver, lead and zinc. 8 km south-south-east from the town of Cobar (the 'Copper City'), the Peak gold mine has historically been a centre of gold and copper exploration with the first version opened in 1896 during the gold boom years. In the late 1980s, the new Peak mines were estimated to contain around 4.5 million tonnes of gold ore.

The company's output remained largely stable in the September 2020 quarter, with some minor adjustments due to lower mine operations and capital costs at the Peak mine. Aurelia's total gold production came in at 30,000 ounces, 9% lower than the previous quarter. The decrease is largely due to a 42% drop in gold grades at Hera with ore sourced from lower grade areas, but this was offset by increased gold grades at Peak.

Similarly, mined ore at Peak has been reduced due to the company's underground mining activities at the nearby high-grade Kairos ore zone. Base metal grades increased at Hera, including the production of zinc (13.3kt) and lead (9.5kt). The mixed Q1 results are not likely to worry Aurelia for too long as ore throughput remained steady at both mines.

Bridging the gap with base metals

Aurelia ended the last quarter with no debt and a cool $104m in extra cash (up from $74m in June) to put toward its planned expansions at various prospects around Peak and Hera – all with equally god-like names. While the outlook for Peak is strong because of improved base metal production and the lead-zinc circuit upgrades, the company believes that base metal production will become the dominant revenue contributor at Hera as gold grades are reduced and All-In Sustaining Costs (AISC) increase. The FY21 outlook is A$1,750-2,000 per ounce, up from just A$1,150 in FY20.

Aurelia's next target at Hera is the Federation prospect, just 10 km south, where a June 2020 Mineral Resource estimate showed 2.6 million tonnes at 0.8 grams per tonne gold with an average Net Smelter Return (NSR) of A$343 per tonne. What's a Net Smelter Return got to do with a Mineral Resource estimate? Well, when mines are polymetallic, it helps mine operators calculate the value of a resource when no one commodity predominates. A$343/t is a very nice NSR to have.

Aurelia is excited about the Federation prospect as it is one of the most significant discoveries in the Cobar region, and recent high-grade drill intercepts (including 21.6 metres at 31.9 grams per tonne gold) have suggested a deep gold corridor. The company will incorporate the Federation's results into its next resource estimate while it considers development options at the site.

Aurelia bullish on its gold-dominant trajectory

As its strategy is to become a trusted mid-tier gold explorer, Aurelia is much more concerned with its longevity ('margins over volumes') than becoming a fleeting success story. Despite an 18% decrease in NPAT in FY20 the company has so far managed to maximise profits from its existing operations at Peak and Hera to expand and develop other prospects. And with $104m in cash it seems the company is on track to do that. That cash enabled the company to release a fully franked dividend of 2 cents per share in 2020, totalling A$17.5m. Pretty good for a Pandemic year.

Aurelia's diversity with its lead-zinc-silver by-products is also paying off, thanks largely to the upgrade of its lead-zinc circuit at the Peak processing facility. Even with the gold price starting to deflate a little – now around US$1,900 per ounce - Aurelia is clear on its trajectory as a gold-dominated business with the benefit of those by-products. Current 2020 gold contracts mean that Aurelia is well-positioned to benefit from the price of gold in an ever-volatile market. With the Federation deposit, the company can continue to leverage its assets in the Cobar Basin by extending the mine life at Hera. All of which suggests this stock is four stars.

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Is SK1 the main prize?

Oklo's primary focus for 2020 has been resource definition drilling at its Seko prospect within Dandoko. The project's shining result was unearthing 120 grams per tonne gold at the SK1 North trend, one of Seko's five augur trends (SKI-5), in the March quarter. Since then, Oklo has successfully extended the SK1 to Koko trend to 3m, with test-work still ongoing. Dandoko, as an underexplored gold corridor 15 km in length, sits in close proximity to the rich Senegal-Mali Shear Zone, a region busy with tier 1 gold mines.

Oklo is now one of the largest landowners in west Mali after increasing its ownership of the Kossaya and Sari projects (both within 5 km of Dandoko) to 100% in mid-2020. The company's decision to divest 80% of its non-core south Mali projects to Marvel Gold (ASX: MVL) hasn't come as much of a surprise with the discovery at SK1, now Oklo's preferred target. As Seko presents as a shallow ore body with depths of up to 200m, there is potential for an open-pit mine. The JORC Mineral Resource Estimate (MRE) is anticipated by the end of 2020.

Oklo and others not concerned about politics

While it hasn't stopped companies like Oklo from continuing their exploration, Mali's political tensions could be an ongoing concern for investors after a military coup in August. Sanctions have been placed against Mali by ECOWAS (the Economic Community of West African States), which doesn't bode well for some export/import operations now that borders are closed. That said, the interim government now in charge understands the importance of gold to Mali. The country is now the third-biggest African gold producer thanks to an open policy toward foreign mining investments. So, while there is a precedent for the August 2020 event (most recently the coup in 2012), Oklo is positive any instability in the capital will have little effect on Mali's gold mines in the long-term. That capital, Bamako, is about 500 km away, so in one sense Oklo is a long way from trouble.

The proliferation of institutional mining companies now operating throughout Mali says a lot about the country's serious efforts in recent years to formalise the industry. Mali has been criticised in the past for allowing informal gold production from artisanal mining, so the popularity of western Mali for foreign companies may help to influence more transparent mining policies to help the country prosper from its gold resources. Up-and-comers, like Oklo, as well as major gold producers will be hoping that the recent instability doesn't hinder further growth in Mali's mining industry.

Oklo concentrating on strong investor support

Now that the wet season is over in western Mali, the September quarter will underscore the all-important Mineral Resource Estimate at Dandoko with an expanded reverse circulation and diamond drilling campaign to speed up evaluations at SK1. Oklo is well-funded with $20m to complete drilling, metallurgical work and early scoping studies into 2021.

Oklo firmly believes it has a potential 'company-maker' in Dandoko. The recent drill results suggest similarities in shallow, high-grade mineralisation to B2Gold's nearby Fekola Mine and Anaconda Area. While there's no timetable as yet for a fully realised gold mine operation, Oklo is just as confident in its institutional investor support as it is its results and it's clear big investors feel the same way, with Resolute Mining and Blackrock Group backing the company at 11.9% and 10.8% respectively. Saving any outright political disaster in Mali, for which there is little precedent, we have no doubt that Oklo will continue on the road to potential Dandoko riches. Four stars from us.

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Share price chart

Source: Tradingview

Deep Yellow waiting in the wings

When Paladin Energy was founded in the last uranium cycle, there weren't that many publicly listed uranium miners. Uranium had only been mined by government directive for military purposes or by diversified multi-national majors. From a junior's perspective in 1993, Paladin – and its founder John Borshoff – saw an opportunity to exploit uranium resources with a modern conventional operation despite a contrarian attitude to uranium mining. The expertise behind Paladin arguably turned Langer Heinrich in Namibia into a tier 1 mine. In turn, this paved the way for unrivalled modern uranium miners, like Kazatomprom.

Fast forward a few years and Deep Yellow's flagship project, Tumas Uranium, is set to recreate the same journey from project to tier 1 mine, albeit in a slightly different supply and demand scenario. Tumas is located on the central coast of Namibia, only 60 km from the country's main port at Walvis Bay. A May 2020 resource update for Tumas revealed more than 108 million tonnes ore at 324 parts per million uranium oxide for 77 million pounds of uranium oxide. The company has begun a 90-hole reverse circulation drilling program at Tumas, which will form part of its late-2020 Pre-Feasibility Study. It has already uncovered strong intercepts, including a record assay of 5,820 ppm uranium oxide at Tumas 3. Deep Yellow believes Tumas is similar in mineralisation to Langer Heinrich, which isn't too far away to the east.

We’re going round the twist

The team at Deep Yellow (many of whom are ex-Paladin) have been here before, but you could argue they’ve learned some lessons from Paladin. The strategy behind Deep Yellow is a dual one: focus on Namibia with its straightforward regulations, while constructing a multi-project portfolio. Deep Yellow’s joint venture with Japanese agency JOGMEC at the Nova Uranium Project (directly south of Tumas) is already underway. Aside from expansion activities at Tumas, Deep Yellow says it is well-positioned to benefit from inorganic growth – meaning it has the opportunity to target and acquire smaller uranium projects throughout Namibia and beyond.

As managing director, John Borshoff is still bullish on the likelihood of uranium making a comeback, but admits that most uranium players are ill-prepared to meet the coming challenges – including a widening gap between supply and demand, with demand far outweighing supply by 2040. The likelihood of the uranium price rising to US$60-70 per pound – the amount necessary to realistically incentivise uranium production – may seem slim right now with uranium currently around US$30 a pound. As Borshoff points out, recent production cuts at Cameco and Kazatomprom were not due to lack of supply but lousy contract prices. This is not helped by the fact that there is a tendency to horde reserves of yellow cake on the part of producers. Deep Yellow is hopeful that production cuts (and oncoming fears about lack of supply) will provide a much-needed boost for higher contract prices sooner rather than later.

Another bubble or a long run?

Deep Yellow’s strategy (and surrounding mining environment) is remarkably similar to Paladin’s in that there are fewer active uranium mines or even teams actively involved in uranium today. Like Chernobyl before Paladin, Deep Yellow has to contend with a post-Fukushima uranium stigma and poor uranium prices. Paladin established a portfolio of African uranium mines in the 2003-2007 ‘renaissance’, which were meant to secure supply in the long term before the GFC hit. Deep Yellow is now ready with its expansion strategy in Namibia. But will history repeat itself and produce another Black Swan to derail Borshoff’s long-term view on uranium prices?

In a way, Borshoff is right when he says the utility sector should shoulder some of the pricing burdens, but the market will have the final say. When that demand is realised and uranium’s next run does come along, Deep Yellow and uranium investors will be hoping that enough has been done to evade another bubble.

While we believe that Tumas is a solid three star project with its initial results and Deep Yellow’s bullish attitude, we’re less confident of uranium’s comeback just yet.

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