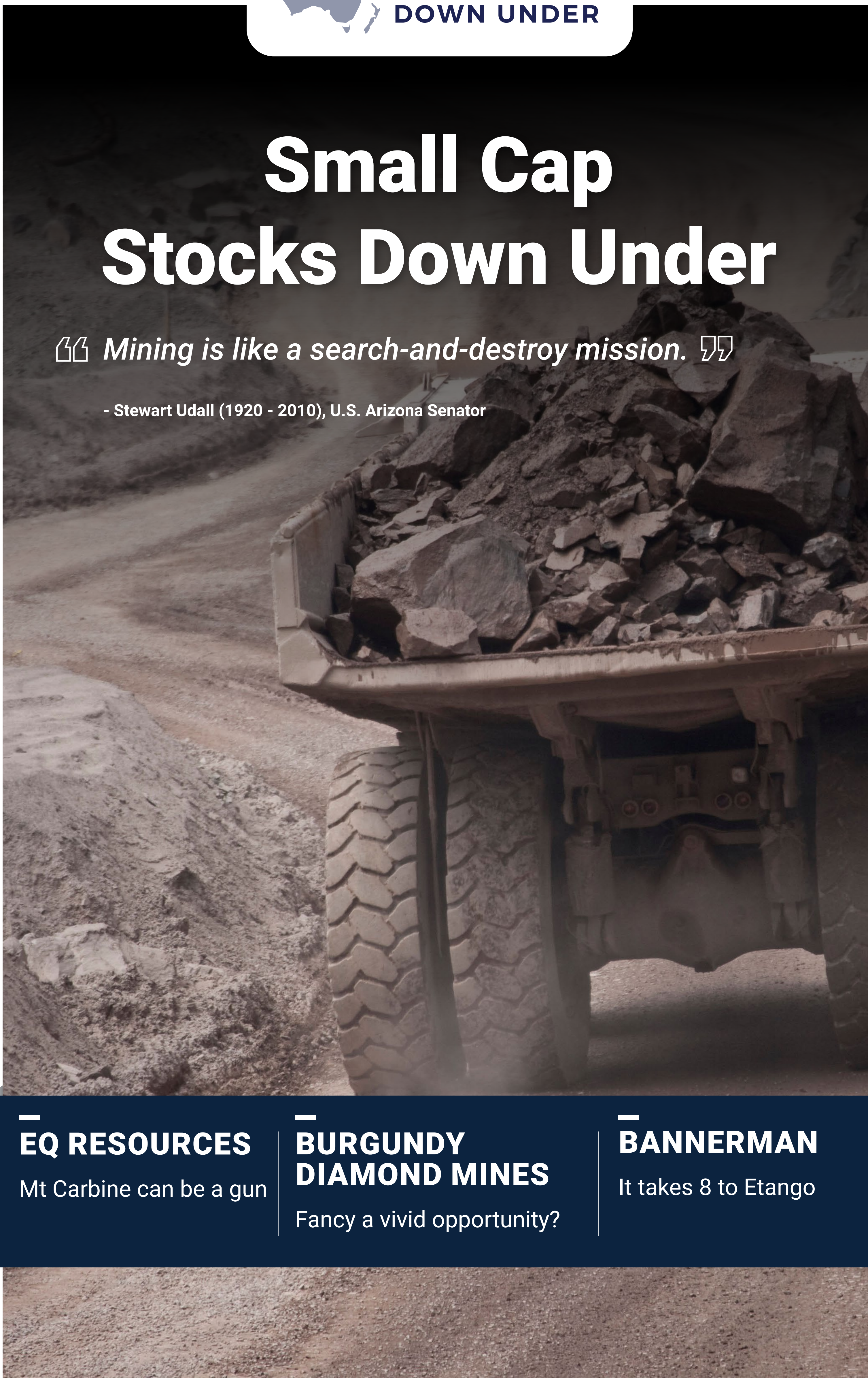
STOCKS DOWN UNDER

3 DECEMBER 2020



Small Cap Stocks Down Under

“Mining is like a search-and-destroy mission.”

- Stewart Udall (1920 - 2010), U.S. Arizona Senator

EQ RESOURCES
Mt Carbine can be a gun

BURGUNDY DIAMOND MINES
Fancy a vivid opportunity?

BANNERMAN
It takes 8 to Etango

EQ RESOURCES

Mt Carbine can be a gun

Stocks Down Under rating: ★★★★

ASX: EQR
Market cap: A$ 35.5M

52-week range: A$0.022 / A$0.059
Share price: A$ 0.032

EQ Resources, whose potential company-maker is the Mt Carbine Tungsten Project in far north Queensland, has seen its stock base-build lately at between 2.3 cents and 3.3 cents per share. We think there's a lot of upside in this one. The medium-term market outlook for tungsten is bright and EQ expects to be able to enjoy early cash flow re-treating existing stockpiles before it moves to hard rock mining at Mt Carbine.

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ASX: BDM
Market cap: A$ 32.3M

52-week range: A$0.03 / A$0.16
Share price: A$ 0.13

It may be that Diamonds are a Girl's Best Friend, as the 1949 musical number suggests, but someone has to make the introductions and that can be a very lucrative business. The Perth-based Burgundy Diamond Mines believes that the global diamond industry is facing a supply shortfall over the next ten years, so now is a good time to be acquiring and developing new diamond projects. It is involved in the Naujaat Diamond Project, the last significant diamond property in Canada not controlled by a mining major. Burgundy will be doing some bulk sampling there in 2021.

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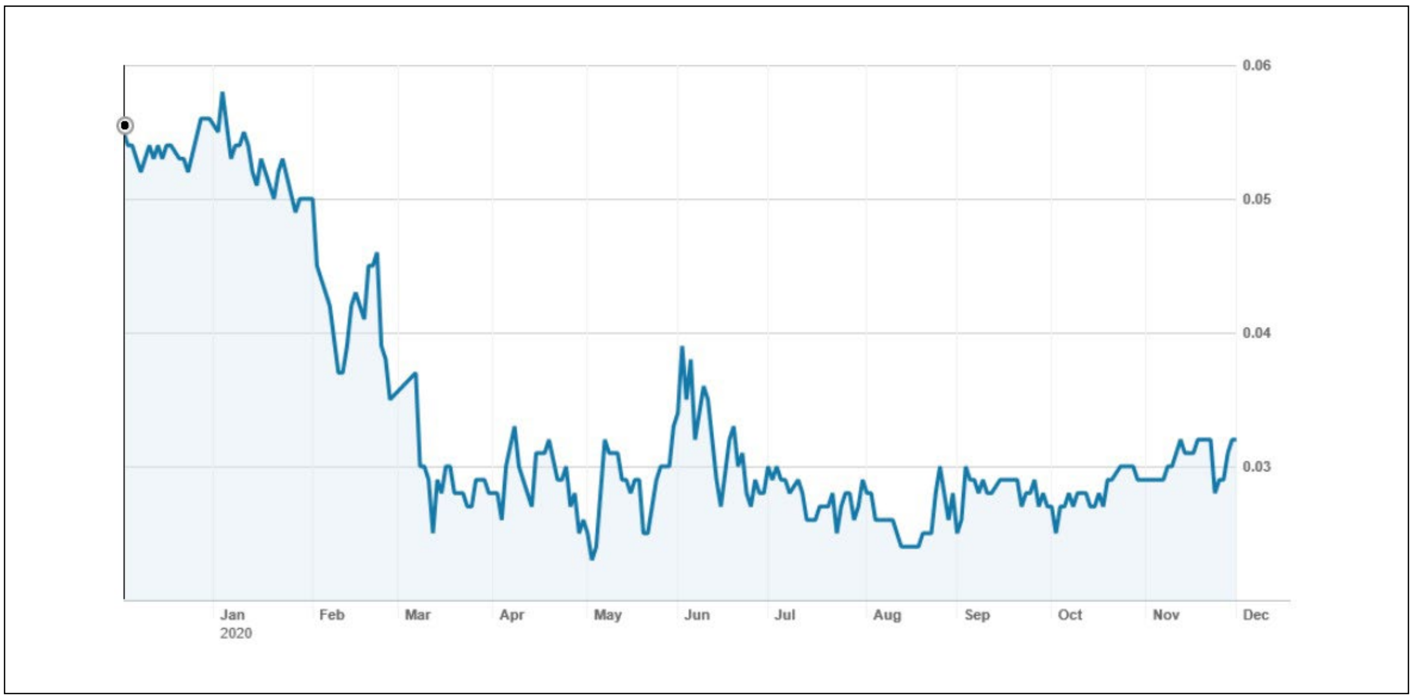
Share price chart



Source: Tradingview

Back on 21 April 2020 we profiled an interesting ASX-listed company called Rafaella Resources, ASX: RFR, which is developing the Santa Comba tin and tungsten project in Spain. Writing that article opened our eyes to the great opportunities available to any company with good tungsten projects in development. Not only is tungsten a vital industrial metal used to convey strength to steel, but there's robust interest on the part of users of the metal in any tungsten available outside the world's dominant supplier, China. For background reading on EQ Resources, another tungsten hopeful, we commend the 21 April article to you, as well as a more comprehensive research report on Rafaella Resources that our sister company Pitt Street Research published on 1 December, and which is available at pittstreetresearch.com.

A tropical paradise… with tungsten mines

If you've ever holidayed at the resort town of Port Douglas in far north Queensland and made the trip up to the world-famous Daintree National Park, you will have been not far from the one-horse town of Mt Carbine, which is about a 65 km drive inland from Port Douglas along Queensland State Routes 44 and 81. The major port city of Cairns is 128 km to the southeast. Mt Carbine sits in an area that has a lot of mining history, including the Palmer River Gold Fields and the Mt Mulligan Coal Field. However, on the town's doorstep is an old tungsten mine. They've been mining tungsten at Mt Carbine on-and-off since it was discovered in 1895, and it was worked as recently as the period 1972 to 1987, where a concentrate of exceptionally high grades was produced before low tungsten prices forced a shutdown. Mt Carbine is actually one of three significant tungsten deposits in the neighbourhood, the other two being the Watershed Tungsten Project, owned by Tungsten Mining (ASX: TGN), and Wolfram Camp, owned by the Canadian tungsten supplier Almonty (TSX: AII).

After close to a decade's worth of work, during which time EQ was called Carbine Tungsten (2011-2017) and Speciality Metas International (2012-2020), EQ Resources wants to restart Mt Carbine and believes it is close. It believes the total replacement cost of the plant and equipment currently on site, as well as the existing 430 metre decline, is worth about A$30m, not much less than the current market capitalisation of the company. EQ also bought a small quarrying operating in 2019, unrelated to the tungsten mine, that supplies material for local infrastructure work. The quarries recently began supplying waste aggregate rock to a regional highway upgrade project and EQ gets about $300,000 a quarter from that activity.

Start small and growth

EQ wants to start at Mt Carbine with an operation that will process tailings. There's now a plant on site that can handle 300,000 tonnes of ore per annum. The flowsheet here is fairly simple, with XRT, that is, X-ray-based sorting followed by beneficiation, expected to extract a lot of ore that couldn't have been easily obtained with 1980s technology. The stockpile's JORC 2012 estimate, which was made in 2014, is 12 million tonnes at 0.07% WO3 (the W stands for wolfram, which is tungsten's other name) for 840,000 mtu (metric tonne unit) of tungsten. That's around ten years' worth of stockpiles based on the size of the plant and EQ intends to start serious pilot plant work from early next year.

Once EQ's new plant is up and running, and earning cash flow alongside the quarries, EQ will use the Mt Carbine decline to recommence underground hard rock mining, with a target of a million tonnes of ore per annum. In 2021, EQ intends to do a complete resource evaluation of Mt Carbine and it believes that the hard rock phase of development can happen as early as 2022. The resource estimate for the main zone hard rock at Mt Carbine is 47.3 million tonnes at 0.12-0.14% WO3 for 6,036,000 mtu. The beautiful part about Mt Carbine is that the deposit is open at depth and to the north, so there's a lot of exploration work that can still be done at the mine site.

The pilot plant work shows promise

Going forward EQ's capital needs are likely to be light. However, the company only had $1.56m in cash as at September 2020. More will be needed to complete the relevant feasibility work on the re-start. However, as a rough guide to the value in this project we reckon the 2012 Feasibility Study, based on stockpiles and open pits (as opposed to the current thinking on underground mining), is as good as any. At that time Carbine Tungsten put an NPV of A$161m on the project, after $55m in capex, and using a price of US$290 per mtu, which is a price within the recent range.

We think expansion of the pilot plant at Mt Carbine through 2021 can help capitalise some of the value suggested by that estimate. With tungsten something that is getting people interested in 2020 and with a lot of work having already gone into unlocking the kind of value suggested by the 2012 Feasibility Study, EQ is four stars for us.

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Share price chart

Source: Tradingview

From the Champion who brought you Riversdale

Back on 28 July in Stocks Down Under we profiled Champion Iron (ASX: CIA), whose company-maker was the Bloom Lake Iron Ore mine in Canada. In late 2015 Champion had acquired an idle Bloom Lake for just C$10.5m, which was A$10.7m at the time. Over the next two and a half years Champion had raised the necessary capital and brought Bloom Lake back into production. By the time we wrote about it, Champion was capitalised at A$1.3bn. That's billion, not million, folks.

There were obviously a lot of people involved in creating all this shareholder value, but an important player was Michael O'Keeffe, Champion's Executive Chairman, an Australian now based in Montreal. Investors were willing to back O'Keeffe in part because he had previously taken Riversdale Mining all the way from A$7m to a A$4bn acquisition by Rio Tinto in 2011 on the back of Mozambiquan coal.

O'Keeffe is a diamond project's best friend

Clearly O'Keeffe knows value in the mining space when he sees it. Which is why investors would be well advised to take a look at Burgundy Diamond Mines, where O'Keeffe currently serves as a non-executive director. If you think about it, Burgundy has a lot in common with Champion Iron. In 2015 iron ore was very unpopular, to the point where good mines were being given away almost for free. In 2020 it's diamonds that are out of favour. Prices declined markedly between 2011 and 2017 and have been low but stabilising since then. You'll recall BHP got out of the game in 2012 when it sold its Ekati mine in Canada and there has been virtually no exploration for diamonds anywhere since then. Burgundy reckons that, with no new mines, there'll be serious deficits in supply by 2030 if long-term demand is any guide. What better time to go and acquire some quality diamond projects than the present? Burgundy did its first diamond deal late last year.

Burgundy's original project, which O'Keeffe vended in, was Nanuk, which is 274 sq km of claims in the frozen north of Quebec to the east of Ungava Bay. That's so far north that Baffin Island isn't far away. The geologists have known for years that there's diamond-bearing dykes on Burgundy's claims, but until now no-one has investigated closely. A dyke is simply a sheet-like body of igneous rock and in Nanuk's case these dykes are partly made of kimberlite, where you often find diamonds. Burgundy will do some soil sampling here soon.

Burgundy knows where to get you some orangey yellows

Nanuk, however, isn't where the action is right now, The company is more excited about the Naujaat Diamond Project in Nunavut, where a farm-in was announced in June. Where in the heck is Nunavut? we hear you ask. Well, if you look on a map of Canada printed before 1999 it won't be there, but it's the vast eastern part of the old Northwest Territories, carved off from those Territories to create a homeland for Canada's Inuit people. The aforementioned Baffin Island is part of Nunavut. Less than 40,000 people live in this Territory, which is about the size of Indonesia, and the capital, Iqaluit, sits at 63 degrees north, so it's fair to say that Nunavut is seriously cold and seriously underpopulated.

The Naujaat Diamond Project covers around 11,000 ha close to a town of the same name. If you're squinting at that pre-1999 map of Canada you'll find Naujaat by its old name of Repulse Bay, at the very top end of Hudson Bay right near Southampton Island. Yes, it's fair to say that Burgundy's potential company maker is in the middle of nowhere.

Early days but promising

What's not nowhere is the diamond potential of Naujaat. Diamonds were actually discovered here by BHP in the early 2000s, but that company never developed the field. It's reportedly good for a type called the 'fancy vivid orangey yellow', the term 'fancy' meaning that the diamonds are outside the normal colour range. Burgundy is now earning 40% in Naujaat from a Canadian company called North Arrow Minerals (TSX-V: NAR) by funding bulk sampling. This is the part of diamond project development where you know diamonds are there but you want to know more about size and quality distribution. Two bulk sampling campaigns and Burgundy reckons Naujaat will be ready for a Scoping Study and Pre-Feasibility Study.

We think Burgundy Diamond Mines is an excellent way to take a position on the expected recovery in diamond prices. Currently, Burgundy intends to add other projects to the two it has in Canada and it recently entered an 'exploration alliance' in Botswana. Obviously it's early days for the evolution of this company but one decent bulk sampling campaign can lead to significant progress. We give this one four stars for investors with patience willing to follow Michael O'Keeffe's leads.

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Share price chart

Source: Tradingview

As we've noted a couple of times lately, if you're looking for a country in which to develop a new uranium mine, go to Namibia. This sparsely populated African country of 2.4 million is comfortable with uranium thanks to long-standing mines there capable of providing 10% of world output. The country's economy is reasonably free. There's excellent infrastructure available to support new mines, including a uranium export facility at the Port of Walvis Bay. And, importantly, the government of President Hage Geingob rates highly on mining-related policy. Now all you need is a decent uranium price...

Needed: Some patience

You also need some patience. Bannerman Resources has been waiting since its April 2005 IPO to get the Etango Uranium Project off the ground. Etango, in the Erongo region of central-western Namibia, is not a remote mine, sitting only about 40 km from the quaint port city of Swakopmund. And it sits where the action is as far as uranium goes. The famed Rössing mine, that got the Namibian industry started in 1976, and its neighbour mine, Husab, are 30 km to the northeast, while the currently idle Langer Heinrich mine of Paladin Energy (ASX: PDN) is about 50 km southeast. On top of these advantages, Etango is pretty big with an estimated resource of 271 million pounds of U3O8. The trouble for Bannerman is that it was first ready to go with Etango in April 2012, when the uranium price was imploding, and the company has struggled to get the economics right ever since.

That said, the 15-year development time is actually an important reason to like Bannerman right now because the company knows so much more about its erstwhile company-maker than it did in 2005. The initial Definitive Feasibility Study from 2012 was optimised in 2015. From 2015 the company did a lot of work perfecting a flowsheet based on heap leaching that improved the project economics and substantially de-risked the project. Then in the middle of this year the company published a scoping study on a cut-down version of the mine, where only 8 million tonnes of ore a year is processed rather than 20 million, but where the capital costs are markedly lower, at only US$254m versus US$870m originally. Bannerman is encouraged enough by the work that went into the 'Etango-8' scoping study to move to a Preliminary Feasibility Study.

A US$212m post-tax NPV

The numbers for Etango-8 look good. In this iteration of Etango the mine produces only 3.5 million pounds of U3O8 on average each year, but at an All-In Sustaining Cost of about US$41 a pound, helped by a low strip ratio of only 1.93:1. At US$65 a pound for the uranium price and after the pre-production capital costs we noted above, that yields a US$212m post-tax NPV at an 8% discount rate. What has Bannerman encouraged by Etango-8 is that it can easily scale into the original Etango-20 if market conditions allow.

Many investors will be wondering what competitive advantage Bannerman has when Langer Heinrich can come back on stream for much less in the way of capital costs (see our 10 November 2020 article on Paladin Energy for more on this). And there are various other players in Namibia with similar projects competing for project financing. Those investors forget Etango's long history, and, that China is now well established in Namibia's uranium industry. There are two main nuclear power companies in China - China National Nuclear (CNN) and China General Nuclear Power (CGNP) – and both of them own Namibian mines. CGNP acquired Husab in 2012 while CNN picked up Rössing from Rio Tinto in 2019. With China continuing to bring new nuclear reactors on stream it's a fair bet that these two mines won't be the last to operate without significant Chinese capital.

Coming soon: US$65 a pound

Now, US$65 a pound is still a while away for uranium, which is why you can currently get Bannerman at a fraction of the Etango-8 NPV. However, US$65 is not unrealistic in the medium term with the emerging structural deficits in uranium supply. There is also the imminent need for many utilities to get back to 3 years of uranium supply under contract after years when the depressed uranium price meant such coverage wasn't a big concern. The fact that uranium went from US$24 to U$34 a pound between March and May 2020, as a result of just a few mines going off-line, is telling you that the market is tightening. It will likely tighten further between now and 2025 when the mine shortfalls are expected to become serious.

Bannerman is now starting work on the Etango-8 PFS and will publish it by mid-2021. Give it another 9-12 months for a DFS and this project could be shovel-ready at a much more propitious time for the uranium price than today. Bannerman was holding A$3.7m cash per the end of September 2020, allowing it to fully-fund the Etango-8 PFS, expected to cost only A$1m. Ahead of this PFS, we think Bannerman and the 'new Etango' is a four star opportunity.

Pitt Street Research Pty Ltd

95 Pitt Street, Sydney, NSW 2000, Australia

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