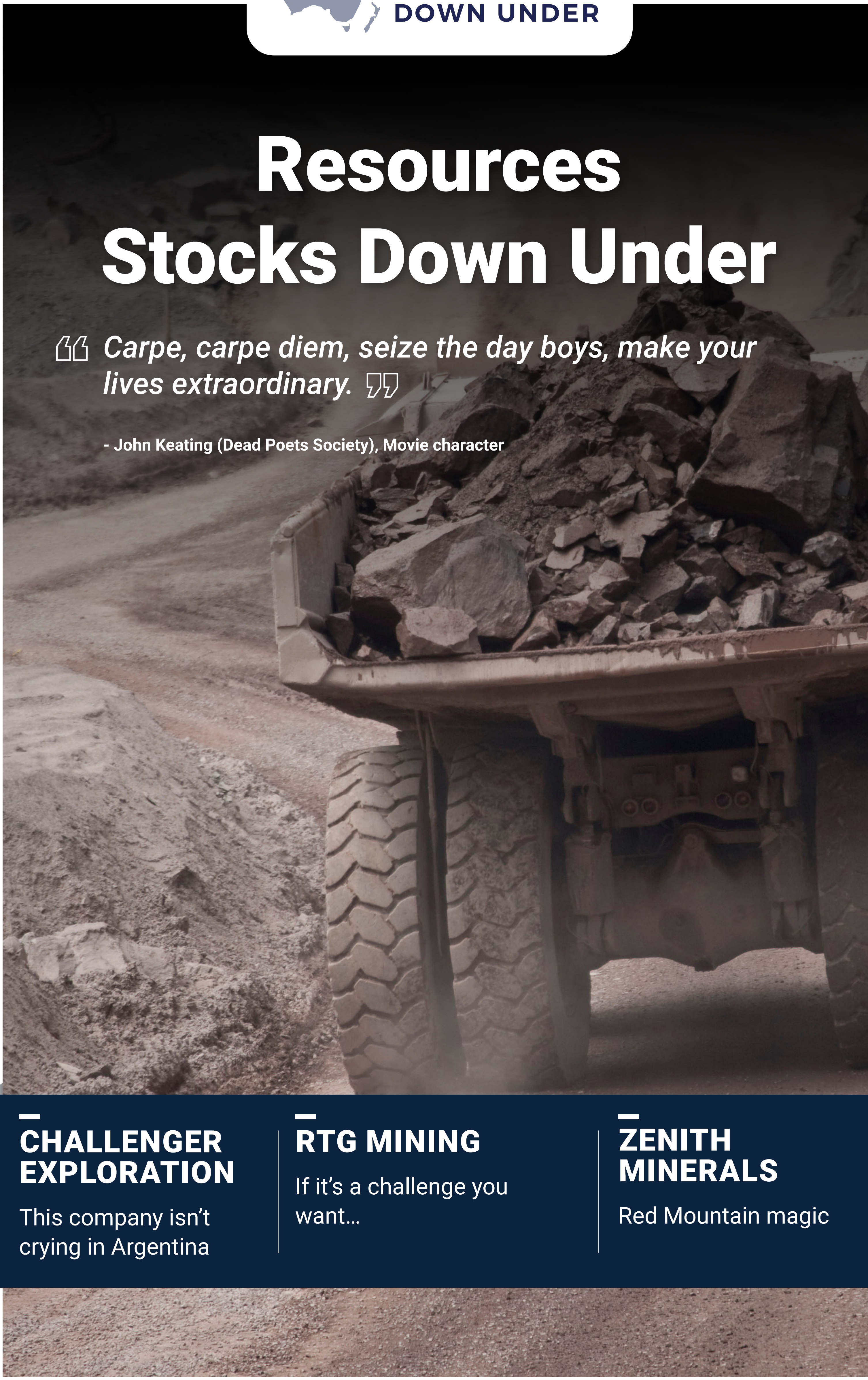
STOCKS DOWN UNDER

27 MAY 2021



Resources Stocks Down Under

“Carpe, carpe diem, seize the day boys, make your lives extraordinary.”

- John Keating (Dead Poets Society), Movie character

CHALLENGER EXPLORATION

This company isn’t crying in Argentina

RTG MINING

If it’s a challenge you want…

ZENITH MINERALS

Red Mountain magic

CHALLENGER EXPLORATION

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Stocks Down Under rating: ★★★★

ASX: CEL
Market cap: A$ 226M

52-week range: A$0.185 / A$0.395
Share price: A$ 0.30

Challenger Exploration is an early-stage explorer with two key South American gold-copper projects: the Hualilan Project in Argentina and the El Guayabo/Colorado V project in Ecuador. Both projects had been underexplored before Challenger got hold of them and what the previous developer missed at Hualilan, the Australian company appears to be uncovering in a serious way.

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Share price: A$ 0.175

RTG Mining, listed on both ASX and TSX, is a mining company with a decidedly emerging market focus, with projects in Mongolia, Tanzania, Ghana and the Philippines. Despite the previous icy relationship between the Duterte government in the Philippines and international miners, plans to remove a ban on mining could assist RTG in its efforts to progress a new copper-gold project. And that might not be the only silver lining for RTG.

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Share price chart

Source: Tradingview

A challenging task

The Hualilan Project, which is located 120 km north-northwest of San Juan in north-western Argentina, is in many ways still a greenfield discovery despite its long history of previous ownership and existing resource. Prior to Challenger making a 75% acquisition from La Rancha Resources, Hualilan hadn't seen any exploration work for over 15 years due to legal issues, meaning no upgrades to a non-JORC resource estimate of 627,000 ounces grading a very high 13.7 g/t gold. Challenger's maiden drilling program provided numerous high-grade intercepts over what is increasingly looking like a large – and previously unrecognised – intrusion-hosted gold system. The project remains open in all directions. That drill programme got the market excited and allowed Challenger to raise $42m at 28 cents per share in May 2021. Challenger now reckons it has a district-scale gold play on its hands and is working multiple rigs to figure out how big this thing can get.

Aggressive exploration is also intended for El Guayabo, although that project is challenging. It's located in the Andean Copper Belt and it is a low-grade, large tonnage site with multiple drill targets around the main Cangrejos deposit, which need to be followed up, including a porphyry system never tested at depth. However, all the action at the moment is at Hualilan. In the March 2021 quarter, Challenger completed a 45,000 metre, five drill rig program at Hualilan and committed to another 30,000 metres. The $42m raise will add another 150,000 metres beyond that and will allow Challenger to move to 100% ownership.

What's the fuss about Hualilan? Basically, the intrusives that Challenger's team are turning up are not just good on the grade front (with intersections such as 39 metres at 5.5 g/t gold and 130.8 metres at 2.3 g/t), but also seem to go a long way in all directions. Challenger suggests a helpful analogy in Newcrest's Cadia mine here in Australia – a high grade starter resource and then a large, but lower grade resource to follow.

Not quite El Dorado

It's difficult to believe such a potential monster could remain so underexplored, especially when it's in gold-friendly San Juan Province. According to Challenger's managing director, Kris Knauer, Argentina remains relatively underexplored for gold exploration by small ASX companies compared to other jurisdictions, like Chile or Ecuador, and this is partially due to the tight hold major US and Canadian companies have on existing gold mines in the region. Even with its extensive drilling history, Hualilan's unofficial resource of 627,000 ounces has resulted in limited production on a smaller scale, but Challenger's initial maiden drilling program seems to be revealing a much larger project. The point is to prove there is at least a 1-million-ounce resource stemming from a significant bulk gold system.

Given that Hualilan and El Guayabo are basically in their infancy as projects, a more defined high-grade, low-capex operation at Hualilan in the near-term is part of Challenger's strategy for what will likely be an even bigger exploration program in Ecuador. Despite the fact that El Guayabo is situated in a Tier 1 gold region surrounded by majors, the project has a similarly sketchy history with Kinross and Odin Mining being the last miners to even hint what the porphyry contains. That leaves Challenger with a lot of unknowns, including the orebody's potential attachment to another 17-million-ounce orebody only 5 km away at Colorado V. The company's geological modelling has so far shown a number of near surface porphyry systems with large undrilled mineralised breccia bodies, so Challenger is effectively treading old ground to find a big discovery.

Best to sit and wait

Challenger describes 2021 as the year to demonstrate Hualilan's true scale and if the last few months are any indication, it has the necessary experience and funds – around $15m in cash – to get the results it wants. Since the last round of positive high-grade results this month, Challenger will continue the 50,000-metre program of drilling, geophysics and scoping with the opportunity to extend that program further to explore every bit of mineralisation it can find.

With that in mind, the company's most pressing focus is all about the news flow to keep its investors happy and provide a reason to top of the exploration fund. It almost goes without saying that Challenger's ambitions lie in becoming a significant producer beyond South America and not just gold production: the company is also eyeing something entirely new at the Karoo Basin Gas Project in South Africa – another underappreciated project with a long history. Challenger is expecting a JORC-compliant resource in the second quarter of 2021. Four stars ahead of this resource upgrade.

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Share price chart

Source: Tradingview

8 is a lucky number

Although its work has spanned across three continents and seven mines, RTG's main game today is the high-grade Mabilo copper-gold project in the Philippines' Camarines Norte Province, on the island of Luzon. Mabilo has a gold equivalent of 1.97 million ounces at 4.8 g/t and 472,000 tonnes at 3.70% copper with a strong copper porphyry at the nearby Nalesbitan deposit offering further exploration upside. The project is at an advanced stage economically, with the project's 2016 Feasibility Study outlining low capital and operating costs and rapid payback at $1,200 per ounce gold and $5,000 per tonne copper. RTG is currently in the final stages of permitting with near-term production anticipated shortly.

This is not RTG's first foray into the Philippines; the company previously developed the Masbate Gold mine, 350 km south of Manilla, through CGA Mining and its partner Filminera Resources. Even with RTG's own track record of successful operations, it was always going to be tricky managing the Filippino government's anti-mining stance – or at least that was what we all thought. But in May 2020, the Mines and Geosciences Bureau awarded the project a mining permit and now the country is in full back flip mode, having just lifted a nine-year moratorium on new mining agreements. RTG's share price responded favourably at the time and that re-rate has more or less held up.

Emerging markets are difficult, to say the least

Such a sudden turnaround is undoubtedly excellent for RTG's chances at Mabilo, especially now that the 10% increase in commodity prices also means a significant increase in the project's Net Present Value, which is now around US$463.2m (substantially more than the US$156m in the DFS). RTG also looks to gain a lot more from the exploration base case following the termination of the joint venture partnership with Galeo Mining.

But it's unlikely that RTG's track record or even Mabilo's potential were the only factors in receiving a mining permit. President Duterte previously expressed his opposition to mining, imposing a ban on open-pit mining in 2017 and further closing or suspending mining permits for 26 mining operations on the basis of environmental regulatory violations. That was before COVID-19. With those pandemic problems ongoing, President Duterte is looking to economic resuscitation through mining.

Subsequent to RTG getting the permit for Mabilo, the project had been temporarily delayed due to a joint venture arbitration with Galeo Mining – which has since gone in RTG's favour – meaning that the company has several reasons (and A$33.6m in rewarded damages) to celebrate this change. Although drilling was curtailed because of the joint venture split, the company believes it can achieve a start-up of operation six months after the start of development, with Stage 1 direct shipping providing net cashflow of US$121m for the first 18 months.

As RTG works in emerging markets, part of its focus is on environmental and social measures – such as its work on Ghana's Oboton Gold mine, which was fully rehabilitated at the end of its life. While that might be enough to sway some sectors of the Philippines, it might not help with the company's ambitious (and controversial) proposal for an exploration license at the Panguna Copper-Gold mine in Bougainville. The Panguna mine, which once provided 45% of PNG's export income, was at the centre of a civil war between 1988 and 1997 over the exploitation of Bougainville's resources for outside gain. As Bougainville is now an autonomous state, the government hopes to reopen the mine and is open as to who does the re-opening (that is, it may not necessarily be Bougainville Copper, ASX: BOC, which we looked at on 31 July 2020). But RTG's negotiations with the Landowners Association (SMLOLA) is already rife with political intrigue.

A is for Audacity

RTG says there are strong parallels between its Panguna proposal and the redevelopment of Masbate, but the company's idea of itself as the frontrunner in this race might be premature given Bougainville's history with other mining companies. While the government wants to generate wealth from the mine, an agreement with SMLOLA will only take place if it directly benefits the community. Compare this with Chanach, a copper and gold project in Kyrgyzstan (that's right – the former Soviet republic not known for being all-that-market friendly these days) and the company has a much easier time with a competitive mining environment, no local ownership requirements and help from China's One Belt, One Road Initiative.

RTG recently raised A$9.2m in a private placement – priced at 5.7 cents a share – to support the advancement of Mabilo. The company is fairly good at creating value from its developments – B2Gold acquired Masbate for US$1.1bn – and the company has a similar purpose for Mabilo. Since previously low copper prices have kept new projects from coming online, Mabilo is suddenly looking much less risky than its other developments, but a significant amount of luck is on RTG's side. While the turnaround at Mabilo is another thumbs up, other development opportunities like Panguna seem ill-conceived, no matter the track record. Four stars.

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Share price chart

Source: Tradingview

Zenith Minerals has yet to find its company-maker. However, if we were to hazard a prediction as to where it will ultimately show up, we'd say Red Mountain. Back in 2016 Zenith Minerals applied for EPM 26384, around 130 km southwest of Gladstone in south-central Queensland. The attraction for Zenith's geologists was its proximity to Cracow, around 50 km further southwest. Gold had first been discovered near this town way back in 1875 and in more recent times the Cracow Gold Mine, tapping a low-sulphidation epithermal gold deposit, had been a foundation asset of Evolution Mining (ASX: EVN). The mine, which over the years has yielded something like 2 million ounces, recently got sold to Aeris Resources (ASX: AIS), a transaction we discussed in our 25 February 2021 article on that company.

How's this for good exploration work?

No previous exploration team has ever thought of Red Mountain as gold-prospective, but after a couple of years of sampling work Zenith knew it was on to something. It decided that Red Mountain was not really a Cracow lookalike so much as it resembled another Evolution mine called Mt Rawdon, which is about 100 km southeast of Red Mountain and within easy driving distance of Bundaberg. At Red Mountain there was a previously unidentified felsic volcanic breccia complex, which the sampling suggested was gold-rich at the edges. That looked a little like the sort of intrusive complexes that had laid down 2.5 million ounces at Mt

Rawdon. The first drilling campaign at Red Mountain to test a 1,200-metre anomaly of interest on the western flank of the breccia pipe initiated in May 2020. The market recovery after the Corona Crash was on so it was a great time to be putting down RC holes.

And what holes! A 17 June 2020 market release reported intersections of 14 metres at 5.5 g/t gold from surface and 15 metres at 3.5 g/t gold from 64 metres. By August it was clear that Red Mountain hosted an exciting zone of near-surface gold mineralisation and the drilling was stepping out from that initial zone. By 13 October the high-grade zone ran for about 300 metres and was open at depth. It was time to bring in the big guns in the form of the diamond drill rigs, which mobilised from late November. By early 2021 it was apparent from the diamond work that the high-grade zone went to 180 metres and, remarkably, visible gold had shown up five times in one hole. The market really liked that when it learned about it on 21 January – Zenith stock quickly went to 16 cents. And there's probably more where that came from because a second diamond drilling campaign kicked off on 21 February, which yielded some good intersections in 14 April and 19 May announcements.

The New Bounty at Southern Cross

Red Mountain isn't the only source of excitement at Zenith. The Split Rocks Gold Project in the Southern Cross region of Western Australia has been generating some good drill results for a while now. The setting is good because the Forrestania Greenstone Belt has historically been generous in terms of its gold endowment. For example, not far away from Split Rocks is an old gold mine called Bounty, which was discovered in the mid-1980s and was a 2-million-ounce producer between the late 1980s and the early 2000s. However, Zenith explorers really only cared about nickel on this project area.

RC drilling by Zenith in 2019 and 2020 at Split Rocks yielded numerous high-grade intersections close to surface. A good example was a 32-metre intersection grading 9.4 g/t gold at a prospect called Dulcie North. That hold was so good, 9 metres of the intersection came in at 31.4 g/t. About 18 targets are now under investigation at Split Rocks and they have yielded some good announcements in 2021.

Funded for the next stage

Then there's Develin Creek. This copper project, 80 km northwest of Rockhampton, is good for copper, zinc, gold and silver in volcanic-hosted massive sulphides. In 2015 Zenith reported an Inferred Resource of 2.57 million tonnes at 1.76% copper, 2.01% zinc, 0.24g/t gold and 9.6 g/t silver for a 2.6% copper equivalent grade. That resource centres on a prospect in the northern part of the project called Sulphide City. However, there are plenty of other prospects that are still being worked up. Drilling at a new prospect, called Snook, in late 2020 recently yielded some good intersections, such as 3m at 1.6% copper, 1.1% zinc and 43 g/t silver. Follow-up drilling kicked off in early May.

We think the market response to Zenith's exploration success at Red Mountain, while broadly favourable since April, hasn't been as strong as was warranted, mainly because gold had been out of favour until recently. That's nothing the next round of drilling can't change. Zenith had $3.1m cash per March 2021. That should get this quality explorer some further mileage with all three of Zenith's core projects. Ahead of what should be a good 2021, Zenith is four stars in our book.

Pitt Street Research Pty Ltd

95 Pitt Street, Sydney, NSW 2000, Australia

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