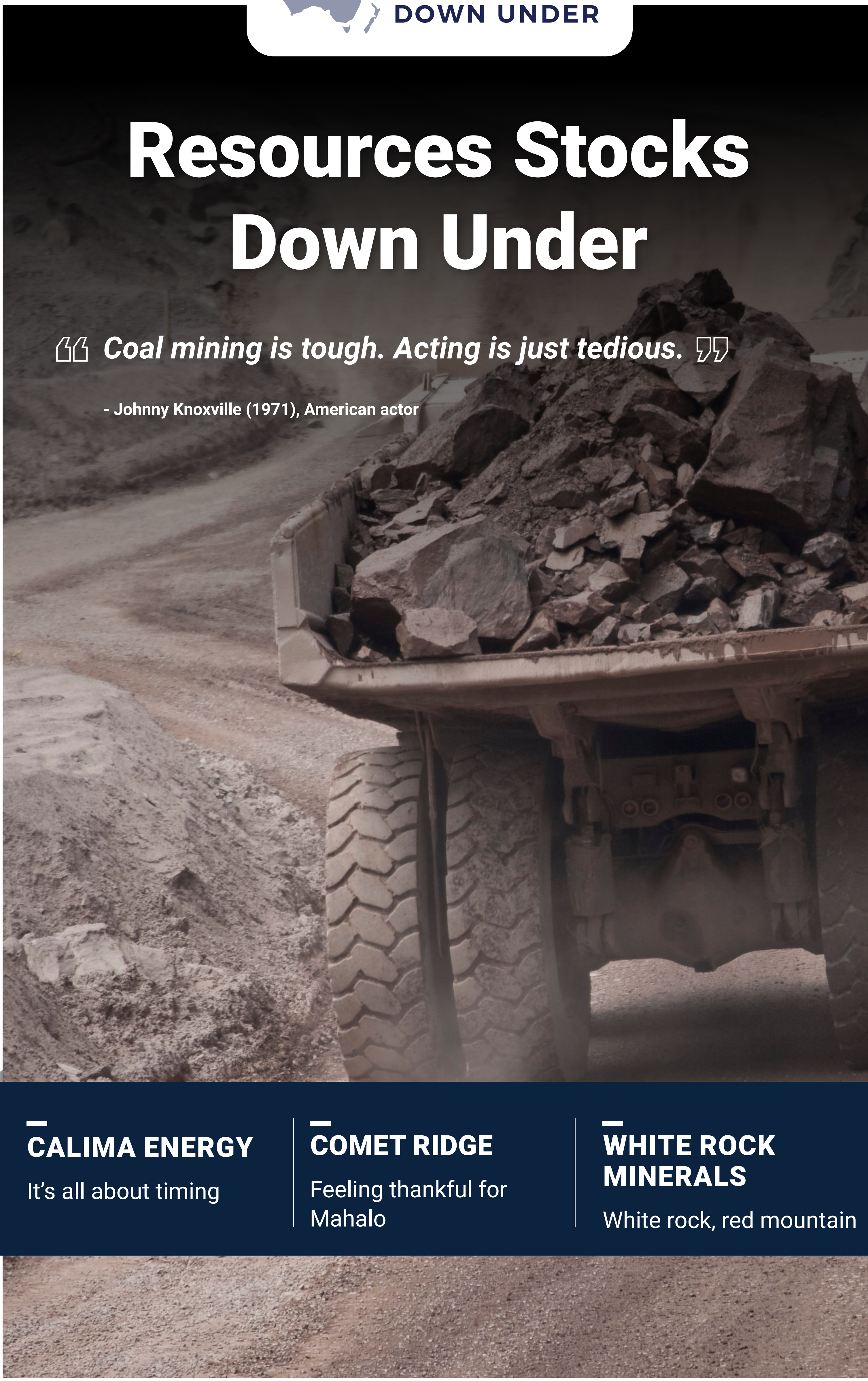
STOCKS DOWN UNDER

9 SEPTEMBER 2021



Resources Stocks Down Under

Coal mining is tough. Acting is just tedious.

- Johnny Knoxville (1971), American actor

CALIMA ENERGY
It's all about timing

COMET RIDGE
Feeling thankful for Mahalo

WHITE ROCK MINERALS
White rock, red mountain

CALIMA ENERGY

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Stocks Down Under rating: ★★★★

ASX: CE1
Market cap: A$ 102M

52-week range: A$0.12 / A$0.24
Share price: A$ 0.19

Since its purchase of a home-grown Canadian oil and gas company, Calima Energy is suddenly an oil and gas producer in its own right with two existing gas plays, Brooks and Thorsby, in western Canada and another, Montney, with development potential. The company has picked up the gauntlet fast, installing four new wells at Brooks with the expectation that first production will start very soon. And that's just one stage of Calima's expansion strategy.

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ASX: COI
Market cap: A$ 83.5M

52-week range: A$0.054 / A$0.115
Share price: A$ 0.099

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Share price chart

Source: Tradingview

Small fish in a big pond

After Calima's Blackspur deal earlier this year, funded by a $38m capital raise at $0.07, Calima basically became an oil producer overnight. Under a binding agreement, the company paid C$4.9m (A$5.3m) in cash and C$12.1m (A$13.2m) in shares to acquire Blackspur Oil Corp, a private Canadian company previously struggling with debts exacerbated by COVID-19 and lower than expected oil prices. Blackspur added the oil-rich Brooks and Thorsby fields in Alberta to Calima's gas-rich, but as-yet-undeveloped Montney Project in British Colombia. More importantly, it brought the seasoned Blackspur team. Calima's Canadian potential just got a whole lot bigger.

After the injection of A$190m into exploration and development, Brooks and Thorsby have a combined 2P (proven and probable) resource of 22 million barrels with a split in the resource base at 71% oil and 28% gas. As Blackspur has drilled 48 wells at Brooks to date, Calima plans to expand production with 24 extra wells to be built over the coming 18 months. So far, the company has extended the output with four new wells (Gemini 1, 2, 3 and 4) targeting the Sunburst formation at Brooks to make use of the current high oil prices and reach its end-of-year production guidance goal of 4,500 boep/d (barrels of equivalent oil per day).

Strict but friendly

For a company only just starting to expand beyond a single project, Calima has lucked out in a big way, acquiring two fully functioning projects for a song. Now that oil prices are set to improve again, there is opportunity to expand all three projects under Canada's strict, but friendly carbon pricing rules. Even before the current expansion campaign, the addition of Brooks and Thorsby presented a promising CY21 financial outlook with an estimated annualised EDITDA of C$25m (A$23m) – at US$60 a barrel – for an output of 3,000 boep/d. But the 9-hole drill campaign could increase output to 5,550 boep/d over the next 18-20 months, bringing the EDITDA to C$58m (A$63m). Since the breakeven point is at US$26 WTI, further production could drive enough profit (if the reserves are there) to eventually monetise Montney. While Canada's carbon tax is rather high – currently C$30 per tonne of GHG, set to be lifted to C$170 per tonne by 2030 – Brooks and Thorsby have the competitive advantage of low CO2 (2%), meaning the need to purchase future carbon credits is reduced.

While the longer-term dream is to go beyond 5,000 boep/d at Thorsby and Brooks, the existing pipeline infrastructure at Montney could give double that if production were to start. In all other respects, Montney is 'development ready' with approval from BC's Oil and Gas Commission to construct a multi-well facility to support the market in eastern Canada and the US. The project's value is evidenced by the recent wave of M&A and joint venture activity in the region, including the advanced and highly anticipated LNG Canada Project. Given this point, Calima remains very open to possible strategic partnerships to improve the project's development, but that can really only happen with secure funding. As the outlook for North American gas pricing looks positive, Calima seems to have entered the market at a very encouraging time.

A much more attractive scenario than a year ago

With a budgeted spend of C$15m (A$16.4m) for the reminder of the year, Calima will continue with its multi-well campaign while it looks to its medium-term growth goal of 5,000 beop/d at Brooks and Thorsby by CY22. Depending on the possible funding support for Montney, the company has an even longer window to reduce its overall debt C$5m in the same period and eventually go beyond 5,500 – 11,000 beop/d in stages. With 11 wells drilled in the Sparky formation at Thorsby, Calima has also identified expansion potential at Nisky and Duvernay Formations.

After the company's recent transformation from emerging explorer to actual producer, Calima's share price is currently sitting around $0.19, but we believe its low operating costs combined with the growth potential at all three plays could see a strengthened share price down the track. Despite Blackspur's early struggles, that team offers Calima a lot of experience in the North American landscape, particularly in regards to Montney's potential as a strategic M&A or joint venture opportunity. And at an EV/EBITDA multiple of just 2x for FY22, which starts in January, we believe Calima stock is very cheap. With improved gas prices and LNG growth on the horizon, we give Calima four stars.

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Doubtless you've heard this prediction before, but it's worth repeating: Within a couple of years there'll start to be noticeable declines in production from the gas fields in Bass Strait that have traditionally supplied a lot of the East Coast needs. That means gas users will need to find alternative sources. It's not just anyone saying that. It's the folks at the Australian Energy Market Operator, who every year assess gas supply and demand and publish their findings in a report optimistically called 'Gas Statement of Opportunities'.

A company-maker in Mahalo

When the blue flames from down south begin to sputter, one notable beneficiary is likely to be the energy major Santos (ASX: STO), which has been investing in new gas projects in Queensland for many years now. And one of the projects that it is likely to step up when Bass Strait steps down is Mahalo, a coal seam gas play in the Bowen Basin. The project sits near the town of Rolleston in Queensland's Central Highlands Region about 330 km southwest of Gladstone. The relevant pipelines that would get the gas into the system aren't far away. The project now has the relevant Federal and state government approvals. And planning is underway for a plant that would produce 70-80 TJ/day. Over the years Santos and its partners have put down in excess of 20 wells at Mahalo and have yet to be disappointed. That is, the gas sits in coals that aren't too far down, the wells have low water production and the gas produced from the wells, when analysed, has been shown to be able to meet the typical customer specifications.

Comet Ridge gets its name from the fact that the Comet River, a part of the Fitzroy River system, flows near Rolleston. The company had farmed into Mahalo around the time of its 2004 IPO and subsequently earned 40%. Until recently, Santos and Australia Pacific LNG (APLNG), the operator of the LNG facility on Curtis Island near Gladstone, each had 30%, but Comet Ridge was the most committed to the project, as evidenced by the fact that since 2019 it has also picked up three large ATPs on the northern side of the original Mahalo Project area, the third of which was formally awarded in May 2021. It's not the only egg in Comet Ridge's basket – the company also has projects in the Galilee Basin in Queensland and the Gunnedah Basin in NSW. But Mahalo is clearly the company-maker if it all works out.

A good reserve position

The evolution of the Mahalo project over the 2004-2019 period meant that Comet Ridge was able to build up a nice reserve position. By late 2019 Comet Ridge's share of Mahalo was 106 PJ in 2P reserves and 183 PJ in 3P. However, that reserve position is set to get even better. In early August 2021 it struck a deal to acquire APLNG's 30% for $20m, $12m at signing and $8m in deferred tranches. The price was low, at only 25 cents a GJ for the 2P and only 15 cents for the 3P. And the funding of the deal was really straightforward – Santos will lend Comet Ridge the money, in return for the right to negotiate its position in Mahalo up to 50%. Santos and Comet Ridge are currently working towards a Final Investment Decision on Mahalo.

The key with coal seam gas projects is that wells need to have good flow rates. In that respect Mahalo has been looking good for about five years. Back in 2014 a vertical well called Mahalo 6 had been drilled and then the Mahalo 7 horizontal well put across it. The aim of the game with coal seam gas is to pump enough water out of the seams so that the gas can be liberated from the coal and flow freely. That can take a while, but when it happens your confidence levels increase markedly. So, when Comet Ridge announced on 3 March 2016 that the flow rate from Mahalo 7 had surpassed 426,000 standard cubic feet a day there would have been champagne corks popping in Brisbane.

The boss is optimistic

Comet Ridge Managing Director Tor McCaul, who has been running this company since 2009, is clearly optimistic about the future of Mahalo. On 13 August he was an on-market buyer of stock. Partly motivating this transaction may have been the view that the market was pricing Comet's Ridge's 2P reserves at way below the level where Origin sold its Ironbark project to APLNG in February 2019. Also, he may have recalled that twice now, in 2009 and again in 2018, Comet Ridge stock has been above $0.40 in environments where gas prices have been favourable and Mahalo has been making demonstrable progress.

We see potential for the stock to do it again barring any major ratcheting down of energy prices, like what we saw last year. And given that Mahalo gets its name from the Hawaiian word for 'thank you', we expect a lot of shareholders will be thankful. Four stars.

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Share price chart

Source: Tradingview

New meets old

Although the company is based in historic Ballarat, White Rock Minerals until recently had only one Australian project and it was a long way north of there. Mt. Carrington, in northern NSW's New England Fold Belt, near the border town of Drake, has for a long time had potential to be Australia's next big silver mine. The district has a long history of gold and silver mines dating back in 1886, with prospecting and small-scale mining continuing into the 1920s. While several small operations produced high-grade gold and silver between 1974-1988, by 1990 most of the ore was depleted and the gold price was too low to continue mining (at US$370 per ounce). About 2008 Rex Minerals set out to revive this field and White Rock Minerals inherited it in 2010 as a spinout company. A decade later Mt. Carrington now hosts an indicated and inferred mineral resource totalling 352,000 ounces gold and 23.2 million ounces silver.

Not long ago White Rock set out to offset the risk of being a single project company. The result was the early-stage, but prospective Red Mountain Project in central Alaska, where there is a polymetallic asset with silver, gold and zinc credits. Located 100 km south of historic Fairbanks – one of Alaska's earliest goldfields – Red Mountain has an inferred mineral resource containing 680,000 tonnes of zinc, 53.5 million ounces of silver and 352,000 ounces of gold. Previous exploration has discovered metal-rich VMS (volcanogenic massive sulphide) mineralisation at two deposits, Dry Creek and West Tundra Flats, while a new gold discovery at the Last Chance prospect could provide a substantial gold resource. White Rock is currently expanding its knowledge of both in its ongoing 10,000 metre RC/DD program.

Two mountains joined by expediency

While the company's 10,000 metre drill program at Red Mountain is designed to expand the high-grade VMS resource already identified at Dry Creek and West Tundra Flats, an IRGS (intrusive-related gold system) at Last Chance could markedly change the picture. Last year's RC drill program uncovered grades as high as 24.8 g/t gold, but prior to these measures the gold discovery remained very well hidden, likely missed during previous exploration over twenty years ago.

The untapped nature of the anomaly (defined by soil sampling as an enormous system west of the VMS mineralisation) provides further opportunity to find the source of the mineralisation within the world-renowned Tintina Gold Belt. And now that the company has demonstrated the down dip potential for the Dry Creek resource to grow along is entire 1,200 metre strike length, another six VMS targets are now on track to be tested. That programme should be fun given the targets have names like Yeti, Yogi and Jack Frost, and there is clearly a lot more to discover. With an April share placement raising close to $8.75m (at $0.51 a share), it's full speed on the 2021 Alaskan work program.

White Rock is not taking any chances regarding its chances and has taken first steps toward a joint venture at its Australian project. With an updated Prefeasibility Study in 2020 for Mt. Carrington demonstrating the potential of a 5-year open pit operation for the production of 166,000 ounces gold, the company has now signed a three-stage agreement with Thomson Resources (ASX: TMZ | watch our 12 August 2021 interview TMZ's chairman). With its silver focus, TMZ will add Mt. Carrington to its growing suite of silver projects with the right to earn up to 70% of the project if it can free-carry the project through the Definitive Feasibility Study and approvals stages before a final investment decision (FID). The staged cash payments of $1.4m ($12.5m at FID) could reasonably help fast track an open-pit development.

Turning point

White Rock's joint venture with TMZ is not the only steppingstone for the company now that it has successfully implemented an all-scrip merger with Victorian developer AuStar Gold. That company not only came with a very large and unexplored land package in the Woods Point-Walhalla field, 120 km east of Melbourne, but early production from the high-grade Morning Star mine. Many investors will not have realised that White Rock now has a shot at bringing back to life one of the richest gold fields in Victoria.

White Rock Minerals has been out of favour for a long time. The market briefly started showing an interest in mid-2020 when the silver price re-rated, but that faded quickly and neither the announcement of the AuStar merger in February 2021, nor the May 2021 farm-in agreement with Thomson related to Mt. Carrington, had anyone all that excited. We think the market will change its mind once it realises that not only is White Rock a company in expansion mode, but that its former company maker in Mt. Carrington is finally coming good.

Throw in the potential for good intersections at those VMS targets on Red Mountain, and White Rock has a lot going for it. We say wait for the stock to stabilise and then look at it as a four-star opportunity.

Pitt Street Research Pty Ltd

95 Pitt Street, Sydney, NSW 2000, Australia