The Sydney Contrarian Financial Analysis

Stock Valuation Report

Aurelia Metals Limited (ASX: AMI)

Date	8/03/2019
Classification	Mid-Tier Gold Miner
Current Price	$0.900
No. Issued Stocks (m)	867.9
Net Cash + Bullion ($ m)	$107.87
Last Dividend Payment ($ p.a.)	$0.000
Market Capitalisation ($ m)	$781.09
Enterprise Value ($ m)	$673.22

Ranking	**Undervalued**
Price Range	$0.815-$1.25
Annual Production Guidance (oz p.a.)	200 000-220 000
All-In Sustaining Cost Guidance ($/oz)	$900-$1 000
EV/AISC-Adjusted Production Guidance ($/oz)	$3,046.00
EV/AISC-Adjusted Production Range ($/oz)	$3 000-$4 000
Resources (oz)	770,935
Reserves (oz)	364,138

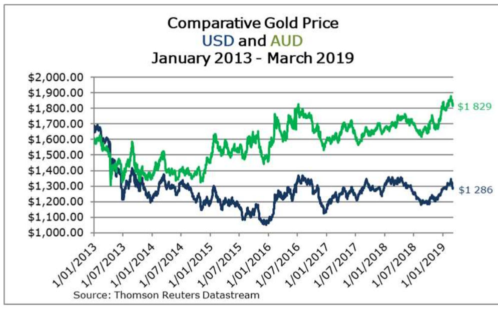
Summary

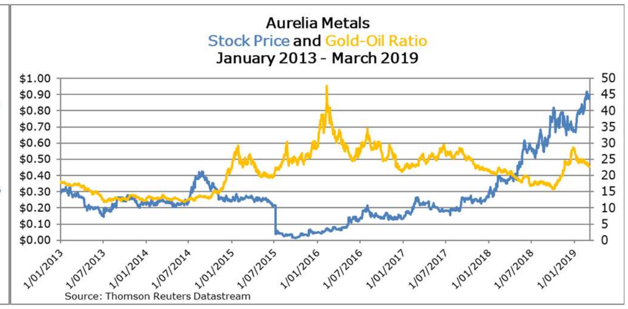
Aurelia Metals is a mining company that produces gold, silver, copper, lead and zinc in the Cobar region in New South Wales. Currently, the company has two operating mines – Hera and Peak, that produced 97 374oz of gold in 2018 (exceeding the 75 000-90 000oz guidance) and is targeting 110 000-130 000oz for 2019 (upgraded from 100 000-125 000oz of gold), or 200 000-220 000oz gold equivalent.

The company has had a volatile run in the past four years as a result of near bankruptcy arising from their debt with Glencore incurred in the process of developing the Hera mine in 2013 (commenced production in late 2014). The company recapitalised in late 2015 and again consolidated in late 2017 with an equity issue of $70m and a $45m loan that was partly to repay their $105m debt as well as funding their acquisition of Peak Mines for US$58m (A$70m). Aurelia was trading in negative equity position as late as the end of the 2017 financial year. Interestingly, the company was generating positive net operating cash flows during the 2016 and 2017 financial years, providing them with a solid case for Glencore to extend the debt maturity. After the Peak mine acquisition in late 2017, the company's fortunes changed dramatically. By early July 2018, the entire Glencore debt was fully repaid and the company had $67m cash. The company's turnaround was impressive, although the journey for investors during 2014-2017 was nothing short of a nightmare.

Aurelia has outperformed in 2018 and is on track to outperform for this year as it has produced in the half year 71 333oz gold and 246 580 oz silver. The company has increased its cash balance over this half year by over $40m. Exploration successes in the Peak mine in Peak Deeps and Chronos have yielded over 10m intercepts with gold grades exceeding 1oz/t. The company plans to spend $35m in exploration and development over the 2019 calendar year. Currently the resources and reserves appear low at 771koz of gold and 364koz of gold equivalent (including silver). The expected mine life for both mines are currently 4 years, although expansion of their reserves will likely extend their mine life. After developing Nymagee at Hera, the mine life is expected to increase to 8-9 years with capital spend expected of $20m. For the Peak mine development, the aim is to increase mine life to 6 years initially with the Great Cobar project.

In summary, Aurelia is on track to outperform for 2019 and has a healthy cash balance supported by two highly profitable mine operations. The short mine life at present will be likely to be extended with their proposed development this year. At present they attract a valuation premium relative to the mid-tier gold mining companies. The stock price currently is $0.90, at the lower end of our fair value range of $0.815-$1.25. With mine life extended and projected outperformance, the company's fair value could be boosted in the future.





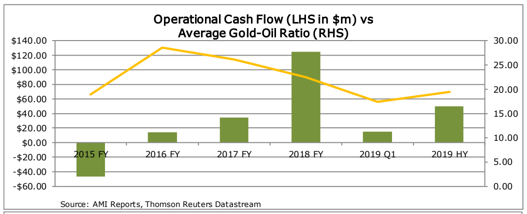
Prevailing Environment

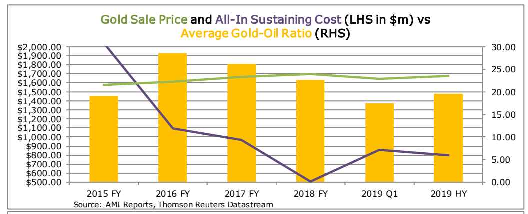
The gold price in AUD terms has branched off increasingly from the USD terms especially in the last three months of 2018 as the Australian dollar declined more sharply, arising from a combination of a flight to safety with the global asset markets peaking as well as confirmation of the slowdown in the property markets in Australia leading to expectations of the Australian economy weakening going forward. Most noteworthy is the gold price in AUD terms was at a record high in intraday trading on 20th February 2019 at $1 878/oz. Two major factors are at play in causing the Australian dollar to remain in the 70-72c range, thus resulting in the gold price in AUD terms to approach the all-time record high. They are the Reserve Bank of Australia announcing in the February meeting that they are uncertain about whether to raise or lower the cash rate and the Royal Commission on Banking final report being released implying further pulling back on credit lending.

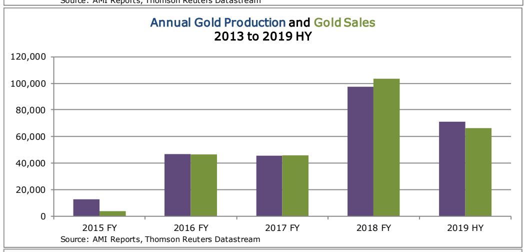
More important to gold mining companies is not so much the gold price, but the relative price of gold and oil. The oil price is relevant as mining companies use large quantities of fuel to power machinery and also the oil price is a significant driver on wages and general costs. A high gold-oil ratio usually results in higher profitability and cash flow generation for gold mining companies.

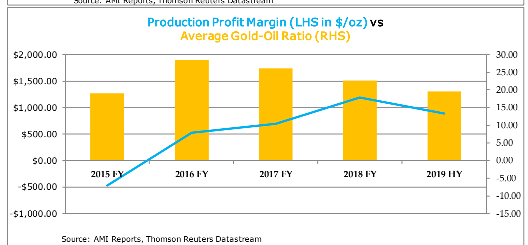
In early October 2018, the gold price began to rally after the September rate hike while the oil price declined, leading to the gold-oil ratio rising from 16 to as much as 28 at the beginning of January 2019. During January 2019, the oil price recovered from the mid-US$40/bbl to US$52-54/bbl, resulting in the gold-oil ratio pulling back to 24. The oil price has recently rallied above US$55/bbl.

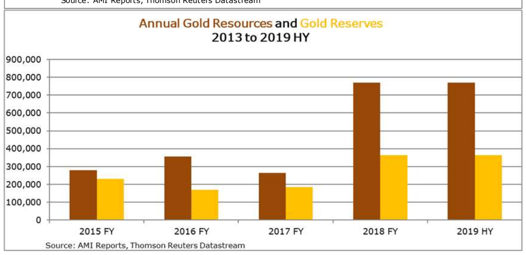
Operational and Financial Performance Charts

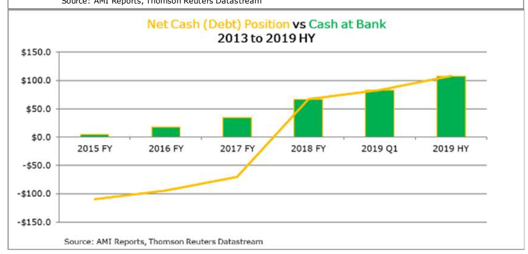








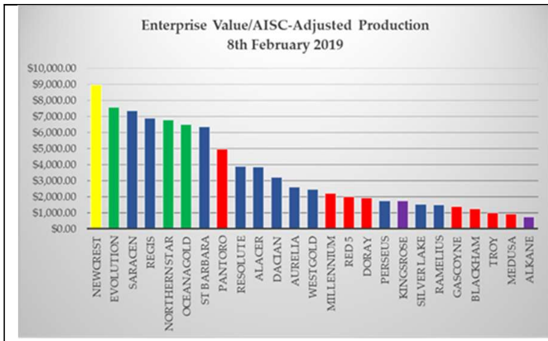


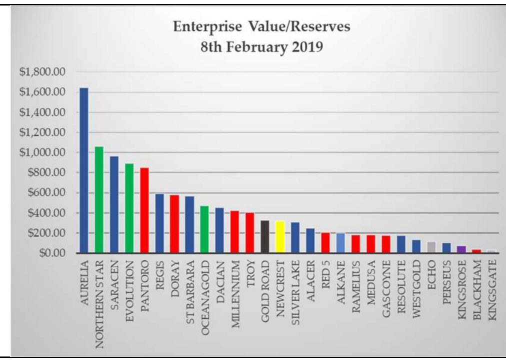


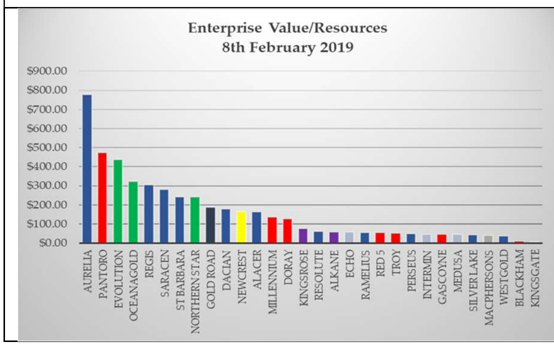
SWOT Analysis

Strengths	**Weaknesses**
• Strong performance in their mines leading to consistent increases in cash balance over the past two years. • Both mines produce silver, copper, lead and zinc that contribute to lower cost of production as a result of by-product credits.	• Concentrated geographic location for its operations in western NSW that can expose them to weather risk. • Resources and reserves are somewhat low for a mid-tier mining company.
Opportunities	**Threats**
• Development of their mines will increase reserves and resources over the coming year and thus increase mine life. • Cash balance may facilitate acquisitions of other mines.	• China slowdown may reduce base metal prices and lead to lower by-product credits. • Climate or natural disaster risks in the Cobar region could cause their operations to cease completely.

Peer Comparison







Glossary

The **Price Range** determines a reasonable range for which the company stock price should be trading at. This range is relatively wide as it considers the *margin of safety*. A company whose stock price is currently outside the fair value range is significantly over or undervalued and investors should look more deeply into the company's operations, financial performance and recent market announcements. This range should not be taken as the sole driver for investment decisions, but as a starting point for further research to identify the potential causes for the current stock price.

EV/AISC-Adjusted Annual Production is a *comparative measure* used for valuing companies in this report and can be used to determine relative value. The enterprise value is the sum of the market value of equity (stock price multiplied by number of issued stocks) and net debt (total borrowings less cash and gold bullion, but excluding gold in circuit and ore stockpiles). The AISC-adjusted annual production is measure whereby the annual production of gold per oz is divided by the AISC adjusted by a factor of 1 000. The intuition behind this measure is to value the company by taking into account annual production but giving favourable treatment for lower AISC and penalising for higher AISC. The factor of 1 000 is arbitrarily chosen. As an illustration, if a company produces 250 000oz p.a. at AISC of $1 250, the AISC-adjusted production is 200 000.

The measure is by no means perfect and other factors should be considered including reserve and resource life, projected production volume and costs, management quality and geographic location. Further, it is of a retrospective nature, focusing on past performance and this may not be a good indicator for future performance.

The **EV/AISC-Adjusted Production Range** is used to determine the Price Range for the company. This range takes into account the baseline range depending on the company's classification, as determined by the annual gold production level. The range can be adjusted upwards or downwards based on other factors that are presented in the SWOT Analysis section.