Australian Gold Fund Valuation and SWOT Analysis

Stock Valuation Report

Blackham Resources (ASX: BLK)

Date	10/05/2019
Classification	Junior Gold Miner
Current Price	$0.010
No. Issued Stocks (m)	3104.2
Net Cash + Bullion + 0.5 x GIC ($ m)	-$4.62
Last Dividend Payment ($ p.a.)	$0.00
Market Capitalisation ($ m)	$31.04
Enterprise Value ($ m)	$35.66

Ranking	**Fair Value**
Price Range	$0.005-$0.018
Annual Production Guidance (oz p.a.)	66 000-68 000
All-In Sustaining Cost Guidance ($/oz)	$1 700
EV/AISC-Adjusted Production Guidance ($/oz)	$892.00
EV/AISC-Adjusted Production Range ($/oz)	$500-$1 500
Resources (oz)	6,715,000
Reserves (oz)	1,530,000

Summary

Blackham Resources is a junior gold producing company with a large 1.53Moz ore reserves and 6.72Moz mineral resources in their Matilda-Wiluna mine in Western Australia. The company delivered their March 2019 quarterly results on 30th April, reporting production of 15 286oz at AISC $1 757/oz. This result was very disappointing as the December quarter forecasted the annual production to be in the 77 000-89 000oz p.a. range due to higher production in the second half of the year. The reduced production was caused by lower mining activity, lower throughput of mined ore and lower recovery rates. While investors expected the company to be fraught with operational difficulties, management did not appear to have prepared investors with this quarter's underperformance. Furthermore, the company undertook on 21st March a highly dilutive 5-for-4 equity issue to raise $25.8m cash, though after expenses would be $24m. The use of these proceeds would be as follows – $10m for operational improvements and exploration, $10m to reduce debt owed to MACA and Lind and $4m would be for working capital management. The company also entered into a toll processing agreement on 29th April with Northern Star Resources (ASX: NST) whereby they would process ore from the Jundee mine in return for fee income. This processing would result in Blackham Resources reducing their annual production guidance to 66 000-68 000oz at AISC $1 700/oz, although they would receive revenue from Northern Star instead.

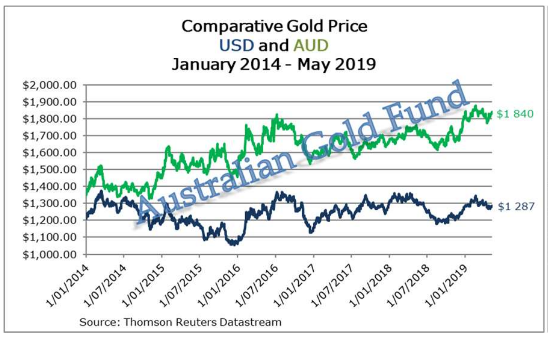
The company's operational woes still are yet to see an end, it appears. The company's ore processing reduced another 14.6% over the quarter to 416kt, and down almost 25% from the June 2018 and September quarters 2018. Furthermore, the ore recovery rate was 75%, well down from the company's track record of 79-92%. Management attributes this to harder ore being processed and that the higher grade ore stockpiles are being depleted. While April recovery rates have increased to 84% and higher grade stockpiles are expected to increase as they source it from the M1 and Golden Age Lower deposits, investors will be forgiven in being sceptical about whether this will indeed be delivered. Mining activity has been less than satisfactory with ore mined being lower than the previous quarter. What is more concerning is the ore grade with the underground ore grade reducing substantially over this quarter from 5.6g/t to 2.9g/t, which is discouraging as the company has been delivering over 7g/t in the past.

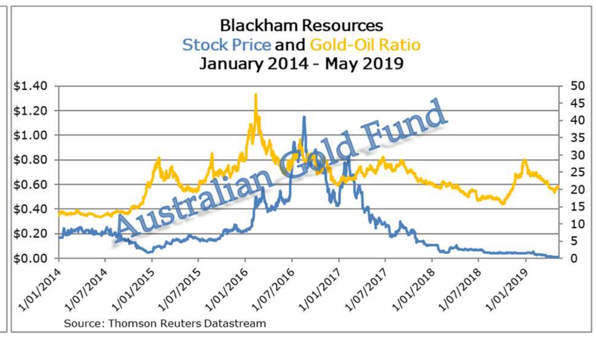
In terms of the company's future development plans, particularly Stage 2 sulfide concentrate sales to bring annual production to 100-120koz, this may provide some hope for investors. The capital raising seeks to support this initiative whereby the company will add a flotation circuit to increase gold production through its sulfide reserves and also seek to sell their sulfide concentrates to interested customers. Management also expects to source their ore from higher grade deposits such as Golden Age Lower, M1 and Williamson. As mentioned before, investor confidence is low and management has a tall order to deliver. Some hope that the replacement CEO to Bryan Dixon, who departed in early May, will be able to step up the game.

https://australiangoldfund.godaddysites.com

The company's financial position since the capital raising has improved. Despite the overwhelming focus on the poor operating results of the quarter, the company's operating cashflow performance was not too poor. After deducting for cashflows from PPE and development but excluding the proceeds from preproduction and exploration, the company's cashflows was $0.26m. The company managed to repay $1m of loans but the cash and bullion position excluding the capital raising reduced from $6.8m to $2.5m, with a net debt position at $21.2m. After including the capital raising, the company's cash balance and net debt position would be estimated at $16.58m and $4.62m, respectively.

The company's operational woes and track record of disappointing shareholders justify a valuation downgrade to $500-$1 500, from $800-$1 800. Given the sharp decline in the company's EV/AISC-Adjusted Production metric to $892, the stock is currently fairly valued. Much trepidation ahead as management is being put on notice to deliver better outcomes going forward.



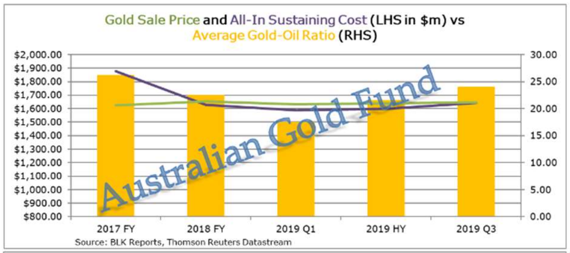


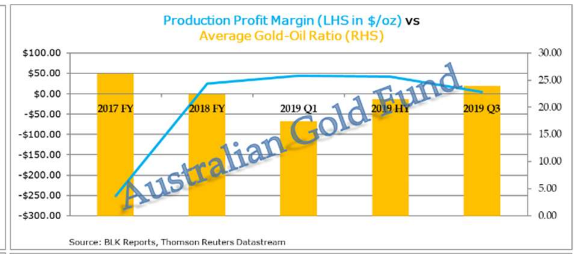
Prevailing Environment

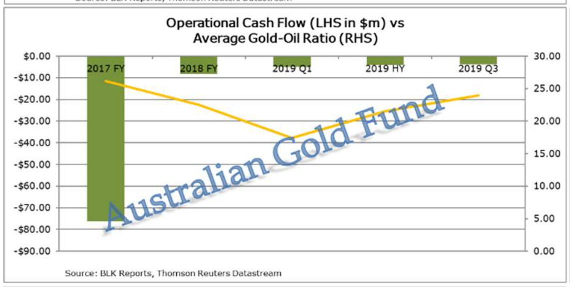
The March quarter has been a challenging one for many gold mining companies despite the gold price trading in the US$1 280-1 345/oz and A$1 790-1 880/oz range. Part of this is caused by the oil price rising 33% from US$45/bbl to US$60/bbl during the quarter, leading to the gold to oil ratio placing some pressure on costs. Since the December 2018 rate rise by the US Federal Reserve that brings the Federal Funds Rate to 2.25-2.5%, the gold price rose to over US$1 300/oz and reached as high as US$1 345/oz in late February. The corresponding rise in the oil price came as a result of higher demand during the northern hemisphere winter as well as increasing geopolitical tension in the Middle East. Furthermore, the oil price rose partly due to reduction in the US inventory. The gold to oil ratio for the March quarter started at a strong 28.3 and gradually fell to 21.5 at the end of the quarter, resulting in an average gold to oil ratio of 23.9 during this period.

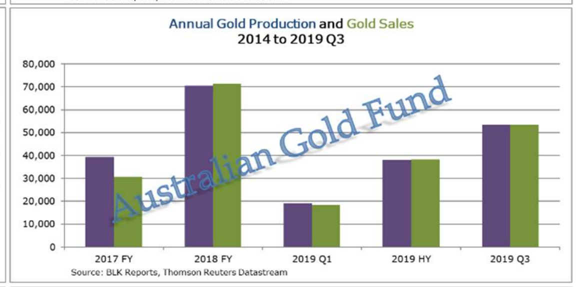
Since the end of the March quarter, the gold price has further weakened while the oil price has increased. The gold to oil ratio has fallen to the 20-21 mark, but there are signs that the gold price is nearing a bottom while the oil price is falling. The months of April and May tend to be cyclical bear periods for gold, with June and July seeing its price recover. This may be repeated in 2019 as the global stock markets are again approaching a peak.

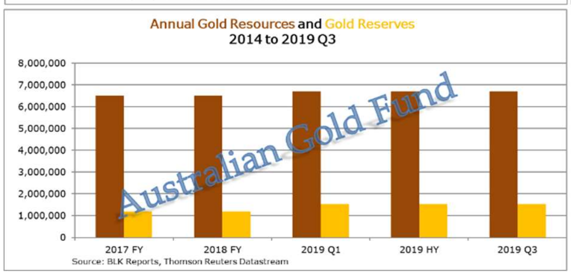
Operational and Financial Performance Charts

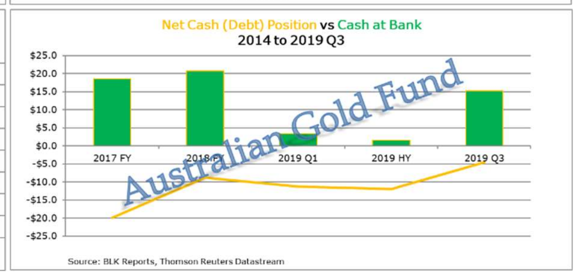








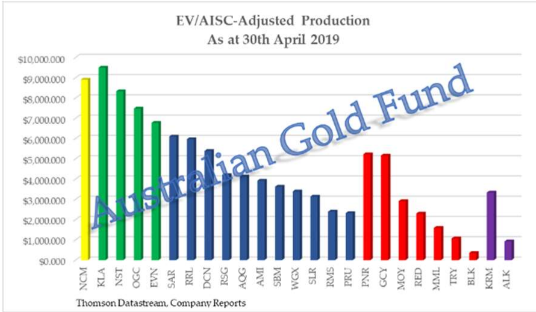


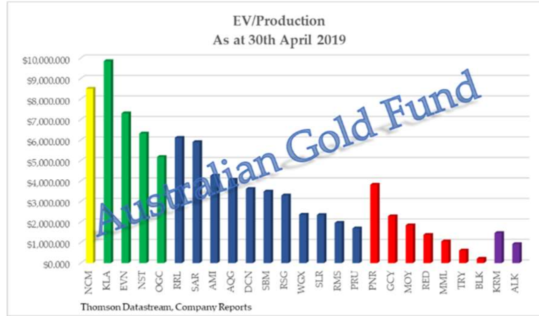


SWOT Analysis

Strengths	Weaknesses
• The mine has substantial reserves and infrastructure that can accommodate a larger scope of production, should it overcome its current obstacles. • Has been able to operate at cash neutral to mildly cashflow negative despite low production volume.	• Tarnished track record of operational issues. • Several external financing campaigns have resulted in substantial dilution of shareholder capital. • Management has developed a reputation of being overtly ambitious about growth prospects and underestimates the need to build a good foundation in their existing operations.
Opportunities	**Threats**
• Negotiation to process Jundee ore for Northern Star signals other companies see their processing plant as being sufficiently reliable, and will generate much-needed revenue and cashflows. • The flotation circuit upgrade may allow the more troublesome sulfide ore to be processed and converted into gold ounces, thus reducing costs. • New CEO hopefully may turn the company fortunes around.	• The Wiluna mine ore may be so difficult to extract, thus leading to commitment of much time and cash with little in return. • Continuing cash burn may finally exhaust the patience of the lenders, MACA and Lind, leading to financial distress should they recall their loans.

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.

Disclaimer

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