Australian Gold Fund Valuation and SWOT Analysis

Regis Resources Limited (ASX: RRL)

Date	9/07/2019
Classification	Mid-Tier Gold Miner
Current Price	$5.490
No. Issued Stocks (m)	507.8
Net Cash + Bullion + 0.5 x GIC ($ m)	$199.43
Last Dividend Payment ($ p.a.)	$0.16
Market Capitalisation ($ m)	$2,787.96
Enterprise Value ($ m)	$2,588.53
Resources (oz)	7,859,000
Reserves (oz)	4,065,000

Ranking	**Fair Value**
Price Range	$3.85-$6.12
2020 *Est* Annual Gold Production Guidance (oz p.a.)	390 000-425 000
2020 *Est* All-In Sustaining Cost Guidance ($/oz)	$950-$1 000
EV/AISC-Adjusted Production Guidance ($/oz)	$6,232.00
EV/AISC-Adjusted Production Range ($/oz)	$4 500-$6 500
EV/Resources ($/oz)	$329.37
EV/Reserves ($/oz)	$636.78

* Estimates are discretionary to include some personal judgment by the author

Summary

Regis Resources is a well-renowned low-cost mid-tier gold mining company. The company has mining operations in Duketon, Western Australia with a development project near Blayney, New South Wales. Regis Resources is currently undertaking the development of underground operations in the Rosemont deposits at the Duketon mines with production expected to commence in the September quarter.

The company delivered 91 087oz of gold in the March quarter at AISC of $1 019/oz, compared with the December 2018 quarter of 90 487oz at AISC of $985/oz. For the financial year, the company has produced 272 453oz at AISC of $976/oz and is on track to deliver on the 2019 full year guidance of 340 000-370 000oz at AISC of $985-1 055/oz. The company does not report the grade of mined ore but reports the volume of ore mined, ore processed and the grade of the processed ore. On average, the company mines 10-11Mt p.a. of ore and processes around the same amount. Despite the low grade of ore processed, the high volume of ore processed provides the company with the economies of scale. For the 2019 financial year, the total ore mined is thus far 7.6Mt (around 75% of annual average) and processed 7.14Mt (around 73% of annual average) of ore at 1.27g/t. Compared to the previous two years, the company looks to be delivering higher grade ore at similar volumes.

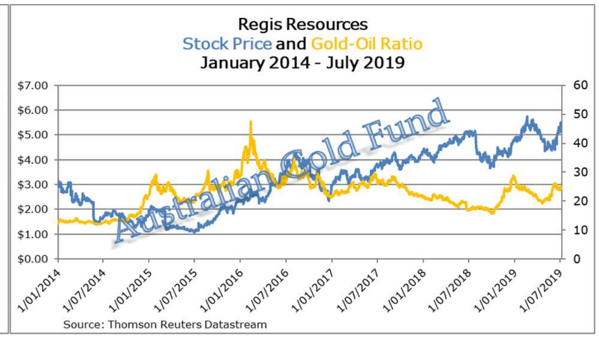
The Duketon North mine comprising Moolart Well looks to be in a steady state of decline with lower mined volume and production. On the other hand, the Duketon South mines have been delivering improving quality ore. In addition, the company has commenced constructing the underground mine infrastructure at Rosemont, where the underground maiden reserves of 123 000oz has been recognised. The mine is expected to cost around $35-40m to complete and will contribute to an additional 480-600kt of ore processed per year. The gold grade from the underground deposits will improve the overall grade processed in the Duketon South operations, and may contribute to lower cost when the operations gain momentum. On a conservative estimate, the Rosemont underground operations may contribute to an additional 50koz p.a. for around 58 months, based on the latest bankable feasibility study figures.

From a financial perspective, Regis Resources has a strong cash balance and bullion equivalent of around $187m. This includes a payment of $0.08 dividend over the quarter, amounting to almost $40m. The company has no debt. The company reports that they have paid around $367m of dividends over the life of the company. This is a notable feat and is rivalled only by Newcrest and Northern Star Mines on the ASX.

Going forward, the company also is proceeding with further review into the development of the McPhillamys gold project at Blayney, NSW. This mine is expected to deliver over 1.7Moz of gold over 9 years of production and will cost around $215m to build. With strong operating cashflow generation averaging $140-$180m p.a., the company should be able to use its existing cash balance and operating

cashflows to finance the mine construction. Dividend payments may vary during this period depending on the company's operational performance.

Based on the current stock price of $5.49, the EV/AISC-Adjusted Production level is around $6 200. This places the company at the upper end of the range. For the 2020 financial year, we estimate the company to produce over 400 000oz p.a. as a result of the Rosemont underground mine also delivering gold. The operating costs are expected to be at similar levels, although mine construction costs may push it above the guidance range of $950-$1 000/oz. As Regis Resources is a strong mid-tier producer and the gold price has now exceeded A$2 000/oz, we have upgraded the valuation range slightly. The company is considered fairly valued.

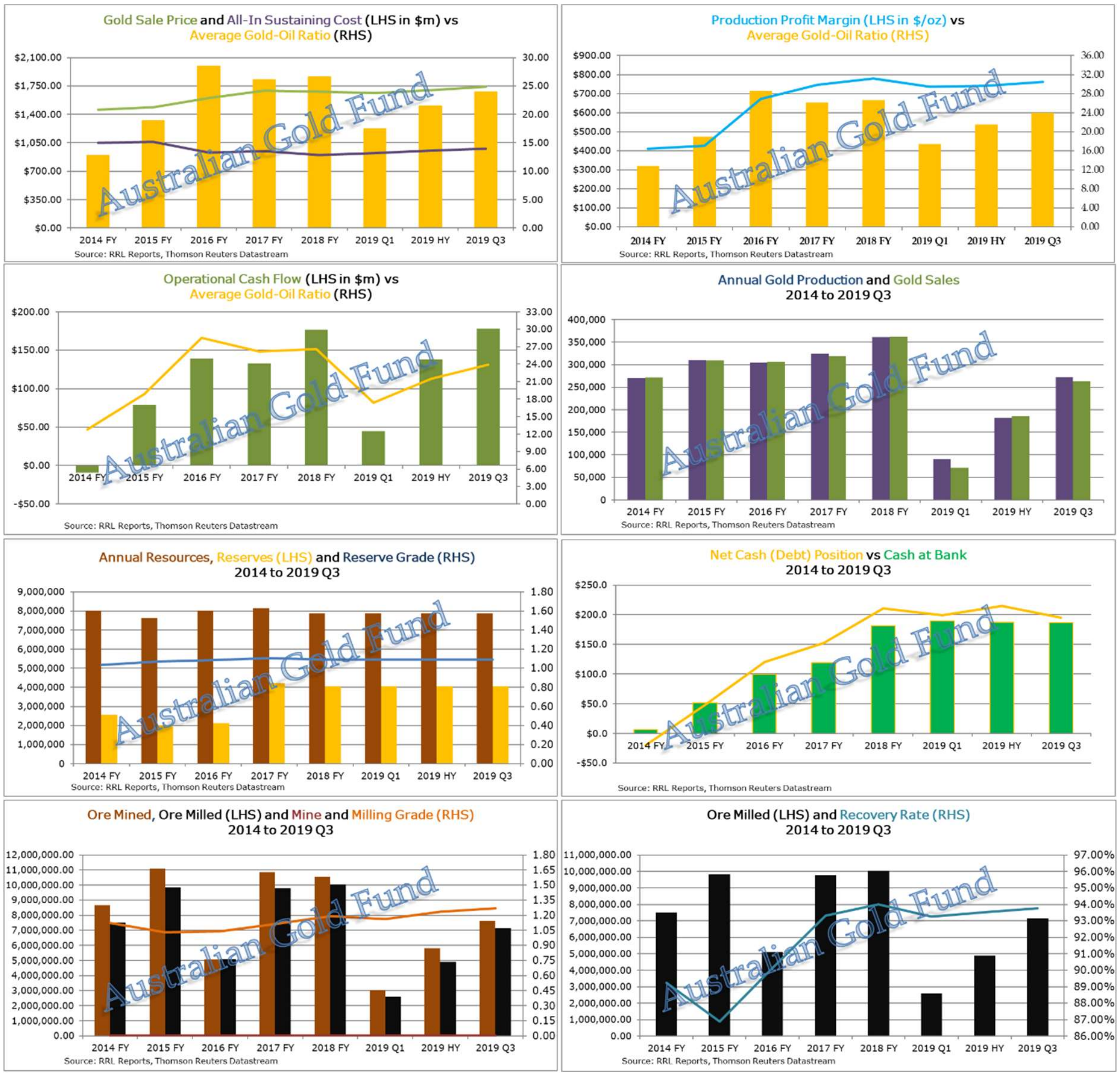


Prevailing Environment

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 weakened to below US$1 300/oz while oil held above US$60/bbl until late May when the US Federal Reserve had a change in tone regarding interest rate rises going forward. Other central banks have indicated rate cuts may occur in the future. Furthermore, the oil price weakened sharply as the US Department of Energy revealed that their crude oil inventory has increased. By mid-June, the gold price has risen to the US$1 330-$1 350/oz range, while breaking the all-time records for the Australian dollar. This extended further on 24th June when the gold price exceeded US$1 400/oz for the first time since 2013. The Australian dollar gold price also exceeded the psychological barrier of $2 000/oz. With oil price in the mid-50's, this is an excellent backdrop for gold and other resources companies to operate. Noting also that the Reserve Bank of Australia has reduced interest rates twice in June and July to 1%, the tailwinds for gold and gold miners will likely continue.

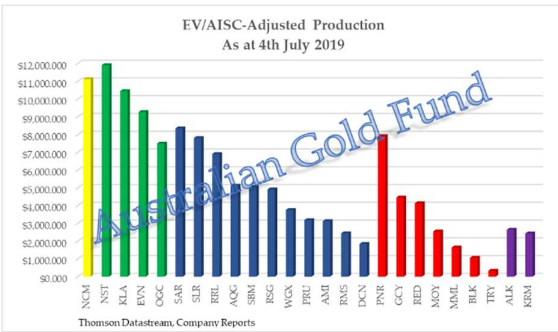
Operational and Financial Performance Charts

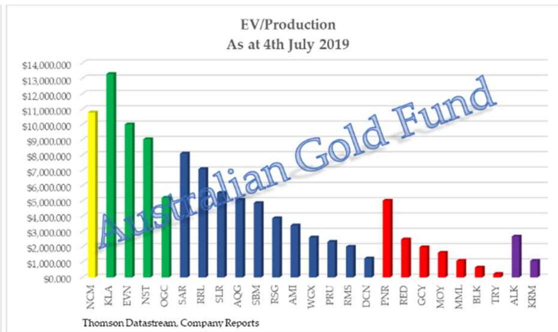


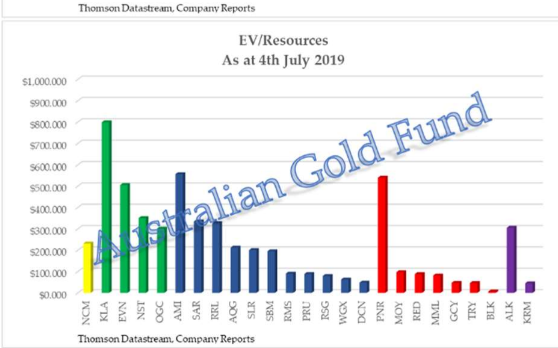
SWOT Analysis

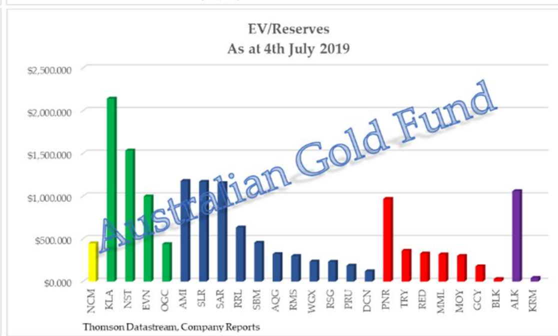
Strengths	**Weaknesses**
• Strong, reliable producing company that has one of the best track records on the ASX and even among international peers. • Reliable cashflow generation and pays a healthy level of dividends. • Rosemont underground and McPhillamys offer exciting growth prospects and can be internally funded.	• Currently valued generously by market investors and may offer less capital growth potential.
Opportunities	**Threats**
• Substantial potential in developing underground mines in their existing properties. • Strong valuation may position them well to acquire other companies.	• Concentration of producing mines in one region.

Peer Comparison









Glossary

The gold mining companies are classified based on their production level on an annual basis. The classification used in this report is as follows – **A** (major producer – 1Moz p.a. or more), **B** (large producer – 0.5-1Moz p.a.), **C** (mid-tier producer – 150 000-500 000oz p.a.), **D** (junior producer – 50 000-150 000oz p.a.) and **E** (micro producer – less than 50 000oz p.a.).

The **All-in Sustaining Cost (AISC)** is a measure adopted by the World Gold Council as a standardised measure of production costs. This cost includes typically the **Cash Cost** associated with the direct production (extraction, transportation, processing and refining costs, staff salary and wages and relevant corporate costs) as well as **Sustaining Expenditure** that may include maintenance of mine equipment and infrastructure, insurance and administration costs over its production life. Companies may still have discretion in apportioning their expenses.

The **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 metric 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.

As a rough guide, the fair value ranges for different mining company classes are as follows:

Major and Large Companies - $6 000-8 000/oz

Mid-Tier Companies - $2 500-5 000/oz

Micro and Junior Companies - $800-1 800/oz

The metric 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 **Net Cash/Debt** is the net amount of cash and bullion the company holds after their borrowings and interest-bearing debt are paid. This represents the liquidity position of the company, although this measure does not consider whether the debt is current (due within the next twelve months) or not. A company in a significant net debt position is owing more than they currently have in cash and bullion, which may potentially put them in financial distress if the debt is due soon.

The **Net Cashflow from Operations Excluding Maintenance Capital Expenditure** measures to what extent the company can generate cashflows from its operations after paying for its operating costs as well as Cash Paid for Purchases of Property, Plant and Equipment and the Cash Paid for Development Expenditure in the Investing Cashflows section of the Statement of Cash Flows. It does not include Cash Paid for Exploration and Evaluation, which is assumed to be growth capital expenditure. This is by no means a stable and comparable measure as different companies may have discretionary interpretation of what constitutes as Operating Activities and Investing Activities or Development, Exploration and Evaluation expenditures.

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.

Disclaimer

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