Monday 8th of March 2021

HALLGARTEN & COMPANY

Portfolio Strategy

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Model Resources Portfolio:

Return of the Carpetbaggers

Performance Review – February 2021

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Model Resources Portfolio

Return of the Carpetbaggers

- + **Some realistic Rare Earth projects are appearing on the scene, most notably that of Energy Fuels (UUUU), but ironically that means bad news for those wannabes that are not serious about production**
- + **Financing activity continued strong with some eye-watering fundings being achieved**
- + **Tin continued its upwards run breaking through $25,000 per tonne before retracing swiftly**
- + **Antimony left its blues well behind it, rising $1,900 in one week and then a further $1,500 in the week after**
- ✘ **Gold had a terrible month sagging back to nearly $1700**
- ✘ **Silver retreated to a lesser extent than gold**
- ✘ **A Bulge Bracket firm's attempt to pump a REE favorite reminds veterans of its efforts with a predecessor firm, that ultimately came to grief**

Rare Earths – Back with a Vengeance

The Rare Earths revival has been building up steam for some time now but in the last two months has gone into total overdrive. As is now the proven pattern the carpetbaggers, both new and old, have appeared from the woodwork like flies following a garbage truck. Some have not realized that "this time it is different" while others are trumpeting their differences.

Some of the old faces have held the course and kept their companies alive through thick or thin. Others, like a particularly notorious example that migrated their mineralogy from REEs to Niobium and now is migrating back, may mean nothing to new investors in the space but to veteran observers these players are freighted with bad vibes.

Notable features of the new tendency are:

- Production is king
- Mid-stream processing is the battlefield now, whereas the first time around it was all about the mine and the mineralogy
- Scant attention is paid to radioactivity. It's an issue that is not going away
- Projects in Canada scarcely figure compared with the first REE boom

- Companies with production (or planned production) in the USA are attracting the most support

There has been a massive cull since 2012, with the supposedly 300 listed REE wannabes winnowed down to a mere 20 survivors. The numbers have picked up slightly since last year, but there is little likelihood of any sort of burgeoning in listed entities as we saw last time. One should also consider that now is quite a different scenario from 2009, when in the wake of the 2008 crash there was a plethora of shells available and not too many competing temptations. Now we have precious metals looking good, copper firing up, battery metals stories and the revived fortunes of weed and crypto acting as siren songs. There are just not a lot of shells lying around on the beach and, in Vancouver in particular, the exchanges are suffering a logjam of listing applications.

The problem for wannabes this time around is that there is little tolerance for the untested greenfield deposit and the exploration thereof. There are more than enough projects nearing (or claiming to be near) production. Moreover there are a number of “killer” projects out there that will negate the economics of new entrants. (This is something we would say about Lithium as well).

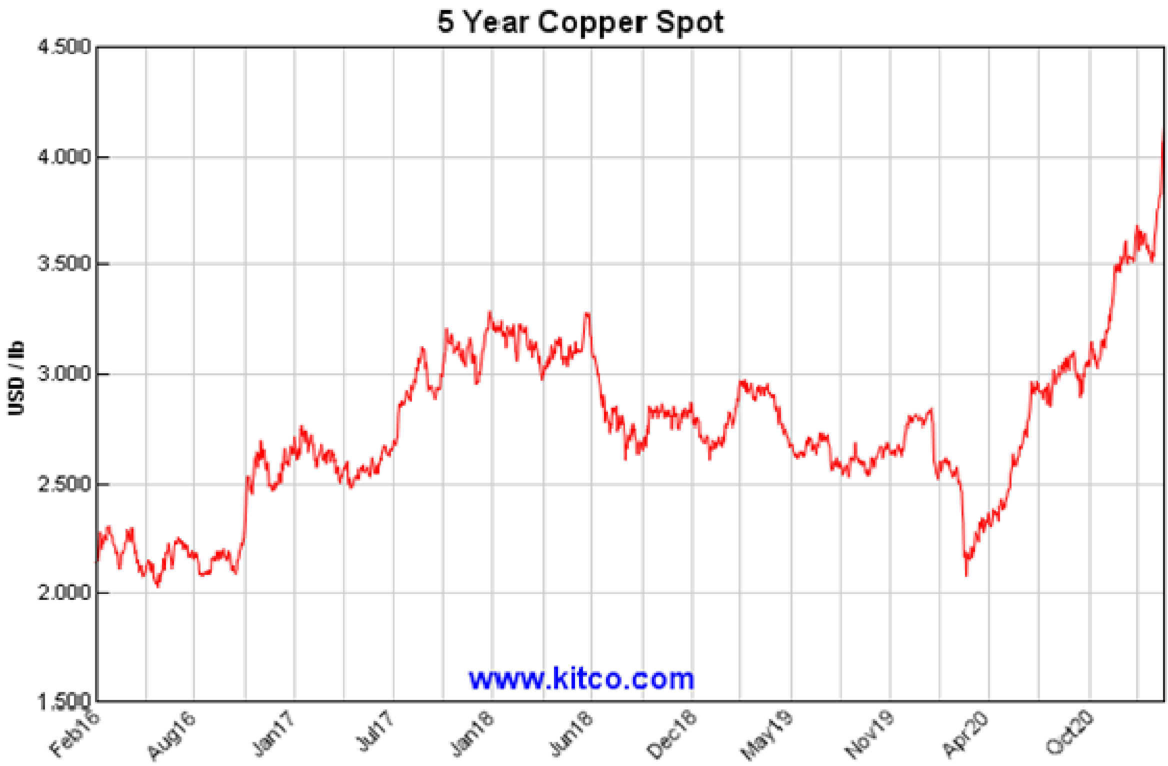
With “economics” being a piece of unknown terminology for the average Vancouver promoter they stand unready to be mugged by events. The appearance on the scene of Energy Fuels (UUUU) has thrown the chess board and all the pieces in the air. While promoters know that you can never have enough (or too much) gold, they fail to grasp that this is not true of REEs, Lithium or graphite. We have already seen one Lithium oversupply scare in the last five years and a real massive oversupply in graphite (caused by Syrah entering the scene). The latter is particularly poignant as a confluence of UUUU, MP Materials and the existing player, Lynas could thwart the ambitions of a whole swathe of REE pretenders with ambitions to get funded and enter production. The last thing these wannabes want is to be declared “surplus to requirements”, as their minerals are then worth nothing either in or out of the ground.

Some of the promotion is trying to compete for the crown of “Most Egregious” title. The cake was really taken though by a Bulge Bracket firm putting a ludicrous target on a particular stock (seemingly) without recalling that they were the same crowd that pumped its predecessor to the skies before changing tack and sending it to oblivion. Wash, and repeat!

Valuations are getting crazy and the SPAC-mania is spilling over into the REE space. This is made easier as most of the US investors into Rare Earths are newbies and don’t have the burnt fingers of Canadian investors from the last go around. This new breed of US investor tends to swallow the mantras that “Rare Earths are rare” and “Washington is serious about resource independence” which ring untrue with most experienced hands. It takes a Molycorp every ten years to reeducate investors (or part a fool from their money) and one can make one’s own guess as to which of the lemons will end up getting juiced.

Red Metal Rising

The recovery in metal’s prices over the last couple of years has followed a curious trajectory, with metals seemingly taking turns to awaken from long (sometimes very long) slumbers and then run before pulling back and consolidating with another metal then taking up the running. Despite its centrality to the industrial economy, Copper has been late to this (supposed) Supercycle Redux, if that is what we are truly in the midst of. Zinc moved up much faster than Copper then paused and pulled back (largely on a strange mass movement of stock into the LME warehouses). Copper though, when it finally caught a tailwind, really flew smashing through the $3 per lb, which had long been a lid on its price, and then swiftly breaking through $4 to reach a high of $4.26, before consolidating.



To us there seemed to be more to this process than just "taking turns". Our long-term perception since the global crisis of 2008 was that China used that event and its traumatic aftermath for the mining sector to mobilise its massive dollar reserves to build up a copper warchest. If worst came to worst it could be consumed as an input.

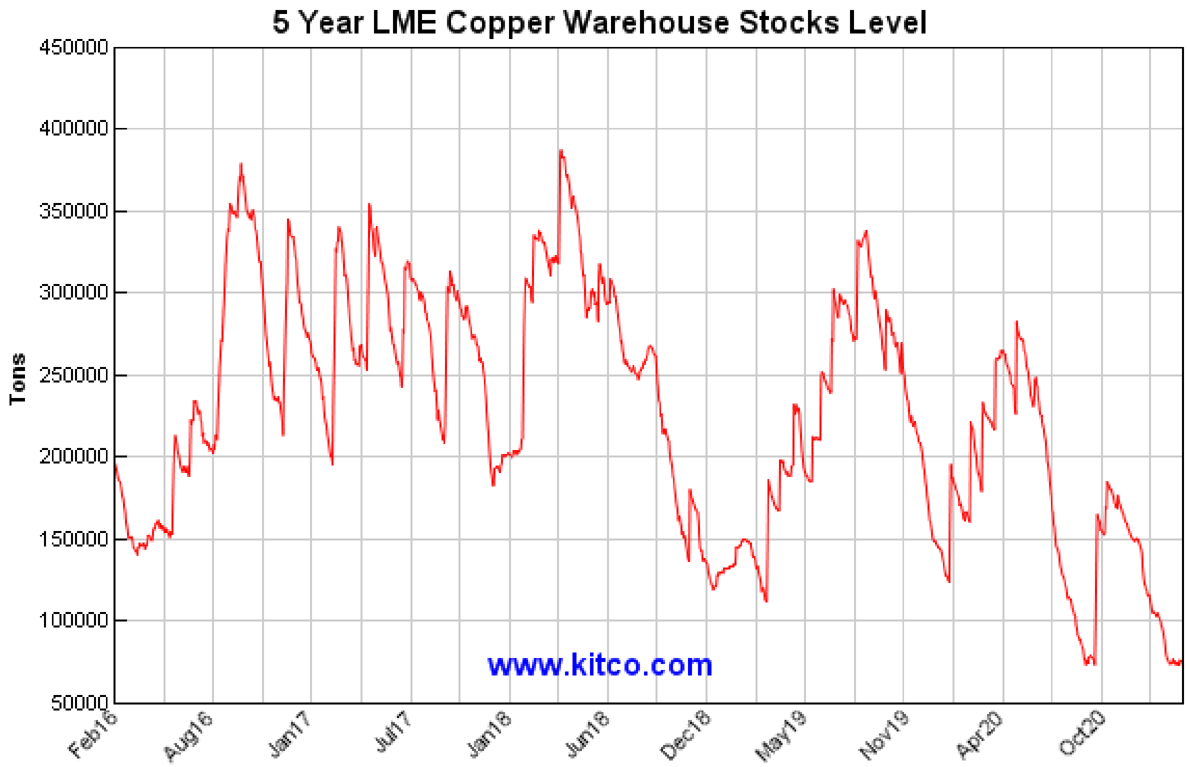
Up until that time the global copper market had been in the hands of the major miners. While the prices did not always work out for them in the way they wanted they had quite a large degree of control over the stock of copper that was "seen" in the markets.

The wrenching effects of the crisis enabled the Chinese with trillions of dollars in accumulated reserves to devote some small part of the financial firepower to start to accumulate sizeable copper stockpiles in unmeasured warehouses and port facilities. Having substantial "undisclosed" stockpiles meant that the Chinese could then add or subtract from exchange warehouses at will and pour cold water on the copper price when it was getting too overheated for Chinese purposes.

Some would dismiss this as mere conspiracy theory. However this period of Chinese control of the Copper price happens to have coincided with the depressed period of the mining sector in general (in a somewhat chicken-and-egg fashion) with the result that the Chinese have been able to position themselves in some of the most sizeable Copper assets under development such as Tenke Fungurume and Las Bambas.

The supply dynamic for Copper has been good (by that we mean it has been bad). Unlike metals like Zinc/Lead and Nickel, there was some copper development during the downtime (e..g. Las Bambas, Constancia etc) but this has been nowhere near sufficient to replace mines that have exited or reduced production and deal with even conservative forecasts of growth in consumption.

The following chart shows the LME warehouse stocks. This shows an interesting seesaw action in recent times. Anyone would think that the trend is down and someone keeps moving in stocks to make it look like a stock build and then it gets slapped down again. That was the trend until recently but now the stocks have been making new lows.



Our conjecture is that China has been living off of the fat of its copper stocks from the Great Accumulation period for some while, but this has resulted in its fire power to bear down on price rises being much reduced. This has made the country vulnerable to the type of surge we have seen since late 2020. It is clear that China is the main loser from this uplift.

So if China no longer has much ammunition in the armoury in terms of stocks of the Red Metal in warehouses (measured & unmeasured) or on docks or in factory yards then the next best thing is copper in the ground. Las Bambas and the interests in the DRC are a start but frankly market control is not made of that. If China had five Las Bambas scattered around the world in friendly (to them) jurisdictions then their firepower might be restored.

How the pushback might manifest itself is not clear, but the Chinese financial firepower is considerable and should not be underrated. But sometimes if one runs out of bullets the best strategy is to sue for peace (i.e. pay up). Something tells us that this is not in the Chinese playbook, as we have seen over and over again (e.g. Tungsten, Vanadium, REEs, Lithium and Copper) where some form of shell-game to signal lower demand is used to sink the price of a desired commodity. Fool me once, shame on you, fool me twice, shame on me.

Portfolio Changes

During the month we added a LONG position in Phoenix Copper.

Galane Gold – Missing an Open Goal

We have mentioned before an unfortunate character of our acquaintance who was so unlucky in his endeavours that it was said that “if he decided to make hats, people would be born without heads”. We are constantly reminded of this when returning to the benighted Galane Gold. The company made frequent appearances in our SHORT lists for its sheer incompetence and ineptitude. We covered out Short a long while ago and the stock has gone up a lot in the last twelve months but that does not mean that anything has really changed, just that a new group of suckers have been found who buy the stock irrespective of its fatal flaws. The company has long wallowed in the comfort of excuses for poor performance and hapless moves with the lackadaisical gold price since 2011 being the prime figleaf management clung onto.

However, the dramatic recovery in the gold price in 2020 has not corresponded with a real recovery in Galane’s fortunes. Now Galane still manages to lose money despite a record gold price and its bottomless well of justifications has run dry.

The table on the following page shows the results over the last few years. It has been largely a litany of misery for the hapless shareholders. Most damning is 3Q20 numbers. Gold hits its peak of around $2050 on the 5th of August, smack bang in the middle of that quarter. What did Galane produce? A loss for the quarter. The company lost money in two of the three quarters it has reported for FY20. The full results for year must be published by May and should in theory be positive. However never let it be thought that Galane can’t seize defeat from the jaws of victory. We are positing a profit after tax of US$2.36mn but we can’t help thinking that we may be proven wrong to the downside.

On the following page can be seen the “progression” of results in recent years:

Galane Gold

In Millions of USD

	FY21e	FY20e	3Q20	2Q20	1Q20	FY19	4Q19	3Q19	2Q19	1Q19	FY18	FY17
Mine Revenue	60.35	51.50	14.93	10.38	9.47	41.40	9.04	12.46	11.42	8.48	44.65	37.30
Cost of Mine Revenue	48.70	40.89	11.39	8.40	8.60	40.57	9.78	10.89	10.60	9.30	41.68	35.56
Gross Profit	11.65	10.61	3.54	1.98	0.87	0.83	-0.74	1.57	0.82	-0.82	2.97	1.74
Selling/General/Admin. Expenses	2.35	2.45	0.61	0.51	0.56	1.70	0.13	0.68	0.22	0.68	2.98	1.88
Exploration	0.10	0.10	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.20	0.21
Depreciation/Amortisation												-
Interest Expense (Income)	5.20	5.20	0.20	1.79	-0.45	2.18	1.45	0.24	0.10	0.38	0.92	2.15
Revaluation of Warrants			2.85					0.20				
Unusual Expense (Income)												0.00
Forex costs (gain)	-0.65	-0.65	0.37	-0.11	-1.23	0.03	0.25	-0.26	-0.08	0.11	-1.63	0.57
Other Operating Expenses	0.80	0.80	0.31	0.18	0.33	0.74	-0.15	0.24	0.41	0.25	0.83	0.23
Total Operating Expense	56.50	48.79	15.74	10.77	7.81	45.22	11.46	11.98	11.26	10.72	44.97	40.60
Operating Income	3.85	2.71	-0.81	-0.39	1.66	-3.82	-2.42	0.48	0.16	-2.25	-0.32	-3.30
Gain (Loss) on Sale of Assets	0	0	0	0	0	0	0	0	0	0	0	0
Income Before Tax	3.85	2.71	-0.81	-0.39	1.66	-3.82	-2.42	0.48	0.16	-2.25	-0.32	-3.30
Tax	0.35	0.35	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Post- Tax Income	3.50	2.36	-0.81	-0.39	1.66	-3.82	-2.42	0.48	0.16	-2.25	-0.32	-3.30
Diluted Weighted Average Shares	230.00	230.00	231.78	223.40	223.40	201.81	201.80	200.80	200.80	200.80	160.27	146.41
Diluted EPS	0.015	0.010	-0.003	-0.002	0.007	-0.019	-0.012	0.002	0.001	-0.011	-0.002	-0.023
Estimated Av. Au Price	$1,880	$1,880	$1,872	$1,716	$1,552	$1,378	$1,580	$1,460	$1,305	$1,291		$1,275
Ounces Au produced	24,700	28,447	7,738	5,691	6,818	30,294	6,839	8,435	8,694	6,326	35,527	29,354
Galaxy concentrate (ozs) 74%	7,400	7,400			952	2,905	2,905					
Ounces Au sold	32,100	35,847	7,974	6,046	6,105	30,950	7,097	8,538	8,750	6,565	35,746	29,896

The problems here, besides the management, are that the mine in Botswana is like an old workhorse being worked to death. The Tau Deeps, as they are called have been showing declining grades, but the company has been exploiting them to the max. This ultimately spells an end to the mine sooner rather than later. Exploration expenditure has been minimal in the six years we have been watching this story so it is no surprise it can never add to its resource or mine life. Then there is the Galaxy Mine which has been a lemon for previous owners and a lemon for Galane at the start, having got into production several years back and then almost immediately been shuttered again due to issues that were never too obvious (though probably the reasons that other bidders were not particularly interested in this asset).

Try as we might we cannot find details of the ounces produced from Galaxy despite the company claiming to be in commercial production. In the past it was publishing a number of ounces in concentrate, which was as clear as mud.

Even with us bordering on the charitable (something Galane does not deserve) we find it difficult to envision the company making any more than a meagre profit in FY20 and its perpetual haplessness, declining grade in Botswana and gold having retreated $300 from its highs does not augur for much better in FY21. Having risen eightfold over the past two years to a market cap of around $68mn currently, there is a clear triumph of hope over experience amongst the fans of this dog. With Botswana winding down and Galaxy always problematical, Galane is on the road to nowhere.

Parting Shot

The chickens are starting to come home to roost on various fronts for the Chinese. We have written before that the onset of the pandemic has done China way more economic damage in the long term by serving as a wake-up call to the chickens in the global henhouse that a fox was in their midst.

Now a year on though other interesting manifestations are appearing. One might have expected that the Biden regime would dial down the tensions with China. Instead the opposite has happened. We would posit that if the pandemic had not served as such a catalyst for global anti-Chinese sentiments the US would have backtracked. The recalcitrant and stonewalling nature of the Chinese response made it impossible for the normally sinosycophantic Democrats to show any sign of weakness on this issue.

More intriguing is on the metals front where the Chinese have seemingly lost control of the price of Copper, Tin and Antimony. The latter is a metal which the Chinese have dominated for over 100 years but where production is plunging within the country and its processors are increasingly reliant upon the “comfort of strangers” (being artisanal miners lacking either reliability of supply or substantial flows). Tin has also run away and Tungsten is in danger of being lost as the new “major” in the Tungsten mining space, Almonty, is progressing towards opening its third mine (in South Korea) as well as a few other developers in the Iberian peninsula advancing to production. China has fruitlessly sat on the Tungsten price for years now trying to scare interlopers away (and advantage its own machine tool industry) and it has not worked.

Then there are Rare Earths where the stiff upper lip is starting to tremble. Foul rumours are circulating that China has lost control of the Heavy Rare Earths space and is now a net importer and the evolution of a Rare Earths industry in the US is happening at a pace that is faster than one can say "Five Year Plan". Things like this were not supposed to happen.

There is a publication called Rare Earth Observer in which they noted in their most recent edition that "China's objectives are:

- China needs unhindered access to foreign rare earth raw materials, in order to keep going and growing in rare earth. Currently this is not guaranteed at all
- China needs to be able to invest in foreign RE miners everywhere, in order to secure supply sources and direct tradeflows, and have currently existing foreign RE investments safe from political barricades
- China needs open markets for its rare earths and it's downstream products, notably permanent magnets, electric motors and electric vehicles
- China may want to test the resolve of the new US-government, if it would prefer if the issue of rare earth would be put to rest again, just like the previous Democrat administration did, after the Pyrrhic victory in the WTO legal battle with China on rare earth export quotas in 2014"

We would agree with these observations, but suspect that China is now just too late. "Sorry we did not mean it" with regard to using resources as a weapon no longer rings true. The rest of the world is arming up in the aforementioned metals and also in the suite of battery metals. Only China's headlock on the DRC gives it an advantage in Cobalt, but in all the rest of the battery metals it is having to go *mano a mano* with Western battery producers to get its hands on Lithium and Graphite supplies. It is now almost a truism in the EV space that an entirely non-Chinese supply chain for batteries (and REE magnets for the engines) will need to be created for the EV "revolution" to avoid China (increasingly seen as a spoiler) shoving a spanner in the works (pardon the pun).

Life was so much simpler when one was King of the Hill. The Chinese Millennium is getting off to a poor start.

MODEL RESOURCES PORTFOLIO @ END FEBRUARY

	Security	Currency	Price	Change last 12 mths	Change last mth	12-mth Target
LONG EQUITIES						
Diversified Large/Mid-Cap	Teck Resources (TECK.B)	CAD	26.63	56%	14%	$22.00
	Hochschild (HOC.L)	GBP	2.10	24%	-8%	£3.40
Uranium	Uranium Participation Corp (U.to)	CAD	4.99	30%	13%	$6.00
	GoviEx (GXU.v)	CAD	0.3	131%	20%	$0.17
Zinc/Lead Plays	WisdomTree Zinc ETF (Zinc.L)	USD	8.67	23%	7%	$9.00
	Myanmar Metals (MYL.ax)	AUD	0.07	40%	-22%	$0.15
	Telson Mining (TSN.V)	CAD	0.31	182%	19%	$0.50
Silver Producer	Excellon Resources (EXN.to)	CAD	3.85	353%	-1%	$5.50
Silver Explorer	Southern Silver Exploration (SSV.v)	CAD	1.18	203%	23%	$0.80
Silver ETF	IShares Silver ETF (SLV)	USD	24.6	46%	-2%	$26.00
Gold Producer	Soma Gold (SOMA.v)	CAD	0.46	411%	21%	$1.20
Coking Coal	Colonial Coal (CAD.v)	CAD	0.72	112%	-3%	$1.10
Project Generator	Altus Strategies (ALS.L)	GBP	0.849	130%	6%	£4.00
Copper Explorers	Panoro Minerals (PML.v)	CAD	0.2	122%	25%	$0.30
	Phoenix Copper (PXC)	GBP	0.418	318%	-8%	£0.65
Tungsten Producer	Almonty Industries (AII.v)	CAD	1.13	113%	51%	$0.90
Vanadium Developer	Vanadium Resources (VR8.ax)	AUD	0.05	67%	25%	$0.05
Lithium	Neometals (NMT.ax)	AUD	0.35	75%	6%	$0.45
	Lithium Power Intl (LPI.ax)	AUD	0.25	-7%	-14%	$0.30
Scandium Developer	Scandium International (SCY.to)	CAD	0.23	188%	-4%	$0.16
Gold Explorer	Cabral Gold (CBR.v)	CAD	0.61	408%	-6%	$0.60
	BTU Metals (BTU.v)	CAD	0.11	-79%	-21%	$0.42
	Gunpoint Exploration (GUN.v)	CAD	0.58	9%	2%	$0.75
	Bold Ventures (BOL.v)	CAD	0.09	80%	-10%	$0.18
Fertilizers	Verde Agritech (NPK.to)	CAD	1.18	203%	23%	$0.90
Cesium et al.	Essential Metals (ESS.ax)	AUD	0.11	1000%	-27%	$0.30
Rare Earths	Northern Minerals (NTU.ax)	AUD	0.04	-20%	-20%	$0.08
	Neo Performance Materials (NEO.to)	CAD	15.98	47%	5%	$14.00
Tin Miner	Alphamin (AFM.v)	CAD	0.52	189%	13%	$0.48
	Metals X (MLX.ax)	AUD	0.21	163%	24%	$0.14
Oil & Gas	Shell A (RDSB.L)	GBP	13.97	-12%	4%	£14.90
Royalties	Elemental Royalties (ELE.v)	CAD	1.35	n/a	-11%	$2.30
SHORT EQUITIES						
Shorts	NioCorp (NIO.to)	CAD	1.32	61%	89%	$0.40
	Texas Mineral Resources (TMRC)	USD	3.94	425%	159%	$0.30
	Abdn Standard Palladium Trust (PALL)	USD	220.99	2%	6%	$180.00

Important disclosures

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