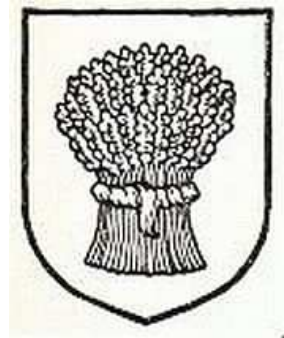


Friday, November 2, 2018



# HALLGARTEN & COMPANY

Portfolio Strategy

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## Model Mining Portfolio: Buying Exploration

Performance Review – October 2018

# Model Mining Portfolio

## Buying Exploration

- + **Base metals prices have a better underpinning, Copper warehouse stocks are declining precipitously, with now only Chinese machinations weighing on prices**
- + **Gold has staged a good rebound, silver less so**
- + **Vanadium is storming higher, in fact so high that its potential use for mass storage may be thwarted before its begun**
- + **Rare Earth inventories have plunged as the EV boom starts to bite, export restrictions and prices rises to follow**
- ✗ **Many players in the EV boom have been resting on their laurels with regard to Cobalt supplies, we repeat this will be the point of maximum vulnerability**
- ✗ **Tungsten prices remain in the dumpster**
- ✗ **Lithium remains in the doldrums presenting many opportunities for bargain buyers. The IPO in HK of Ganfeng was particularly disastrous**

### **“Buy Exploration” – The New “old” Mantra**

The current wave of M&A (more of a ripple than a wave) is being ascribed to “majors” buying up juniors so that they don’t have to do the exploration work themselves. Frankly we can’t see that this is anything new. The great age of exploring by majors ended in 2008 if not before. The 1960s through to the 1990s saw great companies kicking tyres, things that looked like tyres and things without the vaguest resemblance to tyres in the hunt for new discoveries. Much as we look back with fondness to the dearly departed majors like Noranda, we cannot put our hand on our hearts and say that their efforts were focused. The amount of moose pasture that was traversed was epic and the amount of money expended, that could have been paid as dividends to ever-patient shareholders instead, was mountainous.

To say that the current “trend” is new is a stretch. As we’ve noted it’s been essentially the norm since 2008 but it’s been a practice for decades for bigger companies to buy smaller to get their hands on projects for their production pipeline. The difference is whether the major in question has been doing any work of its own to find metal deposits of economic worth. The biggest deal of recent times, the Barrick/Randgold combination has almost nothing to do with snatching another company’s hard fought-for discoveries and much to do with putting an end to Barrick’s chronic cluelessness. With that in mind,

maybe Goldcorp should be next up to be put out of its misery.

There are still hundreds of juniors out there waiting desperately like the Ugly Sisters at the ball for someone to mark their dance card. There is no shortage of potential pipeline filling projects, but there could be. If we discount the no hope projects, the too small projects, the too problematic jurisdictions and managements with unreal expectations (been drinking their own Kool Aid too long) then the number of projects that a larger miner might be interested in falls well below 200 and we suspect that by 2025 many of those projects will have been corralled into majors, consolidators (new majors such as First Quantum has become), potentially dud consolidators (as Capstone has turned out to be) or brought by the current owners, via some miracle, to production or at least development. And then there is the Chinese... increasingly disliked not just by us but by many developing economies' governments for their irksome ways.

The majors have been dining out on work done (and money wasted) by shareholders of juniors since 2000. But there will be an end to this. Already exploration is seen as more of a niche activity for the intellectually addled, than for companies with their heads screwed on. Bonanzas from "find it and they will come" are still few and far between. For a hopeful junior, one's prize asset is more likely to change hands in a bankruptcy court (after the junior's demise) than in some super-profit payday. We would humbly suggest that only after a massive winnowing of the ranks of juniors and projects will their again be a switch of primary attention by investors back to exploration. Even then the model shall have to change. What we had last decade is broken and like Humpty Dumpty there is no putting it back together again.

### **Portfolio Changes**

There have never been as many portfolio changes since the portfolio was originally launched in 2009 as there have been in September and October. The changes were:

- Liquidated our Long position in NevSun. Sold 50,000 shares in NSU.to at CAD\$5.78 per share on the 28<sup>th</sup> of September
- Liquidated our Long position in RNC Minerals. Sold 300,000 shares in RNX.v at CAD 82 cents per share on the 28<sup>th</sup> of September
- Covered our Short position in Bacanora Lithium. Acquired 60,000 shares in BCN.L at GBP 34.25 pence per share on the 28<sup>th</sup> of September
- Opened a Long position in Phoenix Global Mining. Bought 300,000 shares in PGM.L at GBP 35 pence per share on the 28<sup>th</sup> of September
- Opened a Short position in Niocorp. Sold 200,000 shares in NB.to at CAD61 cents per share on the 28<sup>th</sup> of September

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- Added a Long position in the Neomaterials. Bought 15,000 shares in <http://NEO.to> at CAD \$17.32 per share on 25<sup>th</sup> of October
- Added to our Long position in the Uranium Participation Corp. Bought 50,000 shares in TSX:U at CAD \$4.54 per share on 25th of October.
- Added to our Long position in Para Resources. Bought 600,000 shares in PBR.v at CAD 16.5 cents per share on 22<sup>nd</sup> of October
- Added to our Long position in Sherritt International. Bought 180,000 shares in S.to at CAD 72 cents per share on 22<sup>nd</sup> of October
- Added to our Long position in the Zinc ETF. Bought 26,000 shares in ZINC.L at USD \$7.87 per share on 22th of October
- Added to our Long position in Platina Resources. Bought 2,000,000 shares in PGM.ax at AUD 6.5 cts per share on 22<sup>nd</sup> of October
- Added to our Long position in Northern Minerals. Bought 1,000,000 shares in <http://NTU.ax> at AUD 7.8 cts per share on the 22<sup>nd</sup> of October
- Added to our Long position in Metals X. Bought 300,000 shares in <http://MLX.ax> at AUD 49 cts per share on the 22<sup>nd</sup> of October
- Added to our Long position in Neometals. Bought 600,000 shares in NMT.ax at AUD 23.5 cts per share on the 22<sup>nd</sup> of October

### **The Portfolio Move**

We decided to run down a cash balance that had become disturbingly large as a process of taking profits and ditching non-performers made our transactions largely a one-way street in recent times. The portfolio has somewhat wallowed over the last two months as the metals price slump had a disproportionate effect upon the underlying stocks. The Model Mining Portfolio was down from \$4.543mn at the end of August to \$4.221mn at the end of October. Cash was up from \$1.517mn at the end of August to \$1.86mn at the end of September to \$747mn at the end of October.

### **The Portfolio Changes**

How to begin with so many changes... Probably best to start with the disposals first. **Nevsun** is subject to an improved offer from a Chinese group and as it was unlikely that a better offer would be received we exited this situation. We also exited **RNC Minerals** (the old Royal Nickel) which has diversified into Australian gold mining (the Beta-Hunt Mine) which it seemed willing to sell but then the willingness became muddled. It also diluted its holding in the Dumont Nickel project, our original reason for investing, and thus we thought it was appropriate to take the quite meaningful profits we had

accumulated.

Then we resolved to cover our **Bacanora Lithium** Short. This company owns the blighted Sonora project in Mexico and repeated efforts to finance it (including Tesla's on-again, off-again interest) made this a prime candidate for our odium. Its stock price plunged and we took handsome profits on this short position during September.

We also instituted a Short position on **Niocorp**. This wannabe Rare Earth, then Niobium, and now Scandium story had once been well-viewed by us during its Niobium phase. Since then its stock price has been vigorously promoted higher as the prospects of it actually getting developed recede and the distraction of Scandium was dragged in to "confuse the punters". Know nothing investors keep imagining that somehow the gruesomely large capex will be overcome and yet also forget that Niobium giant CBMM will clearly sink the Niobium price to ensure this project is dead in the water. Elk Creek is going nowhere.

The three new Long positions added during the two months were:

**Phoenix Global Mining**, the Idaho copper developer on which we published a full research note in October.

**Neomaterials** the revived Rare Earth processor which has managed to escape the near-death experience of merging with Molycorp and getting away with MCP's Silmet and Magnequench assets, thus ending up stronger than it was before. Revenues are rising, bottom line is leaping higher and it pays a dividend. Wonders will never cease. We shall say more on this next month.

**Platina Resources**, which is a Scandium developer, that we met during the LME week festivities. We had not seen the company since late last decade when it was firmly wedded to a PGM strategy (hence its ticker). It is located in the Scandium triangle in New South Wales in close proximity to CleanTeq and Australian Mines, without those two companies dependence upon Nickel to underpin the economics. We dealt in passing with Platina in our Scandium Review published during the summer.

Then we have the positions where we have bolstered our existing positions:

Uranium has been a flavour this year bust with as yet no actual legal underpinnings for believing there is a change in US import rules on this material. Expectations have gone way ahead of reality. The stocks have tended to benefit more than the physical ETF because the latter reflects reality better. Nevertheless **Uranium Participation Corp** remains our favorite exposure to Uranium. We doubled up our position during October.

**Para Resources** is our favoured gold producer in the Americas and is moving towards the reopening of its Gold Road mine in Arizona in the near future. We doubled the position here also.

**Sherritt International** still labours under the effects of the lame-brained US policy towards Cuba, the

only other source of Cobalt in close proximity to the US and arguably with a much larger Cobalt resource than Canada. We doubled the position here just in case someone points out this reality to the US president.

The London-listed, US\$-denominated **Zinc ETF** is a curious creature but serves the purpose of giving physical exposure to Zinc prices so in their current weakened state we decided to double up here also.

The Australian Rare Earth producer **Northern Minerals** became a producer during October and decided to re-up our position here to ensure we neither missed a belated recognition of its status or a takeover offer from the likes of Lynas.

**Metals X** is one of the largest non-Chinese Tin exposures available as well as being an exposure to copper. We doubled our position here during the month.

Finally there is **Neometals** the Australian lithium producer which is partnered with MinRes and Ganfeng. The company has spoken of an imminent demerger of its Lithium assets. We had a sneaking suspicion that this was directed towards teasing an offer out of Ganfeng to stop a new mid-stream producer appearing on its patch. However the Ganfeng IPO flop meant it raised less money and thus has less room to move. This in turn seems to have slowed Neometal's enthusiasm for its spin-out. In our view it should go ahead and to get more exposure to this we upped our position further in this stock.

#### **Idaho – Phoenix Rising?**

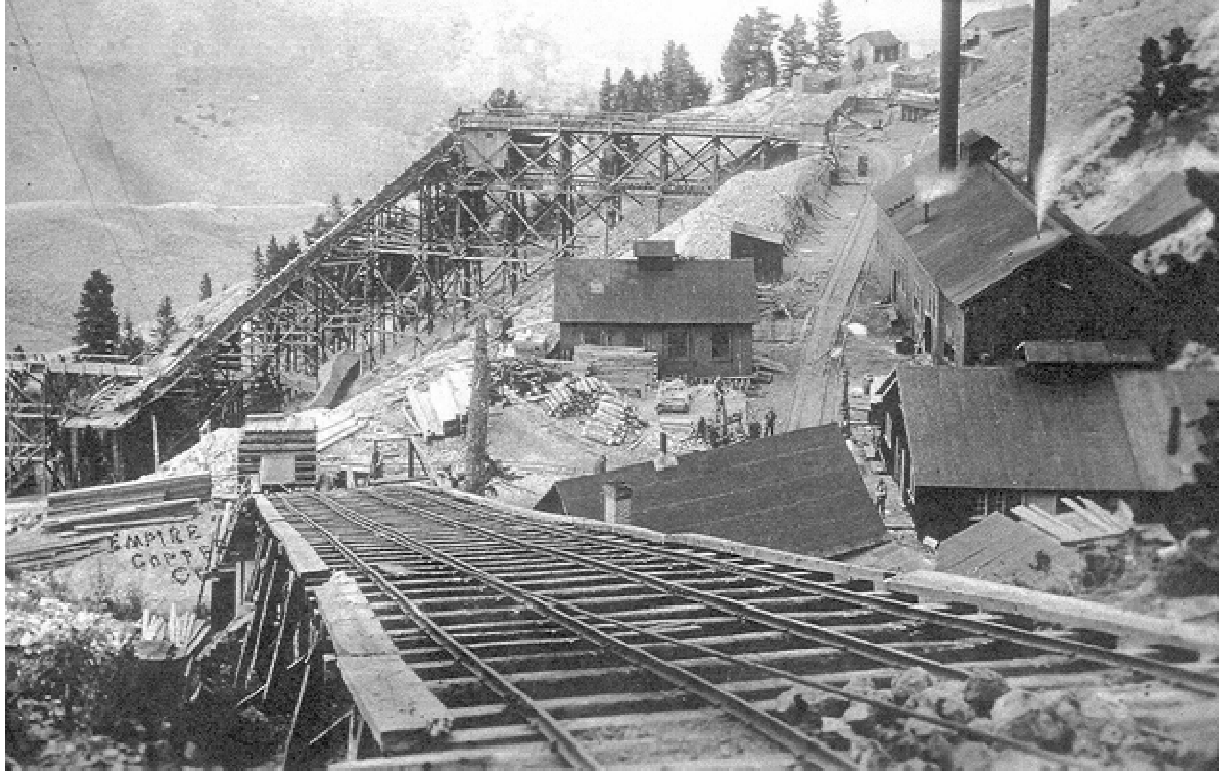
One of our new positions was the copper developer, Phoenix Global Mining which is listed on the AIM and the OTCQB. We will not expound in depth on this here as we produced a major review on the stock during October. Its asset collection consist of the Empire Copper mine in Idaho and a pair of cobalt exploration targets in the hotter-than-the-Majove Idaho Copper Belt and a gold prospect in far north Canada.

The Empire Mine is a former copper/gold/silver producer located in the Alder Creek Mining District in Custer County, central Idaho. The property is approximately 5.5 km southwest of Mackay, Idaho in the Big Lost River Valley between Arco, Idaho and Challis, Idaho.

The property, at the time that Phoenix acquired it, consisted of 23 patented (private) claims, 21 unpatented claims and six unpatented mill-site claims covering a contiguous 301 hectares (743.7 acres). Since then it has been added to, in November 2017, with the Horseshoe claims to the north consisting of 564 acres in 33 claims.

Mineralisation was first discovered at the mine in 1884, when small scale mining quickly commenced and continued through to the 1940s. In the early days of the Empire mine high-grade oxidized ores were mined from open cuts and treated locally in a small smelter. From 1899 to 1907 the mine passed through a period of over-capitalization and mismanagement. The Empire Copper Company acquired the property in 1907 and operated almost continuously from 1907 to 1921, shipping crude ores to Salt Lake

City smelters. Mining underground went on until the 1940s.



Then an open pit was exploited in the late 1970s.

The goal of Phoenix is to start with an open pit and then head underground into the sulphide zone. Recent exploration has thrown up bonanza grades and entirely new zones of mineralisation which have given pause for thought about the originally envisioned processing plan. In the meantime Cobalt sampling results are due and this should dictate whether the Cobalt assets are spun off to capitalize upon the opportunity there. The company is run by veteran mine-builders/operators and not the promotorial types. One to watch.

### **Parting Shot**

It would seem rather elemental to most hedge fund managers that when one takes a large strategic investment one also tries to secure some sort of say in the running of the company one invests in. It had boggled us when earlier this decade it was announced that the funds of John Paulson and those funds (wrongly) attributed to George Soros (who had retired a long time before) made large investments in gold via various instruments and in a couple of the 800lb gorillas of the developer space. We could have been unkind and called them the big dogs of the development space but we never said it out loud at the time.

The push had a certain element of “taking candy from babies” about it and it wasn’t the hedge fund

gurus snatching the candy but the reverse. The years went by and the shirts were slowly stripped from the backs of Masters of the Universe as they came to learn the wisdom of Mark Twain's definition of a mine. They also got to learn that gold is not "as safe as houses" and neither was it going to 10,000 per oz in their lifetimes or even their grandchildren's lifetimes.

Then a little over a month ago we espied that John Paulson had decided to team up with other hefty gold investors in an effort "to work with" management of companies in the gold sector to improve returns, in a combination called the Shareholders Gold Council. In our experience the only way to work with mediocre management in the mining space is to fire them... but let's see how it goes.

The coalition will issue analyst reports and "engage with management" to improve capital allocation, compensation and corporate governance in gold companies. This sounds a bit like applying the electric cattle prod to the soft underparts of mining managements. As we know from experience only the electric cattleprod works. Indeed, the "analyst" reports sound somewhat like the spate of poison-pen Short notes that flooded the market at the end of last decade from "here today/gone tomorrow" operators with weird names like Muddy Waters, spreading the blues on Howe Street and Bay Street.

The initial lineup apparently includes a dozen named investors and four anonymous members. The group includes Adrian Day Asset Management, Apogee Global Advisors, AMG Fondsverwaltung AG, Delbrook Capital, Equinox Partners LP, Equity Management Associates, John Hathaway, Kopernik Global Investors, Livermore Partners, La Mancha and Sun Valley Gold. Maybe one should be even more afraid of who the anonymous members might be, particularly if it's some party like Van Eck.

The Shareholders Gold Council will be headed by Christian Godin, who was recently head of equities and director of research at Canadian fund manager Montrusco Bolton Investments Inc.

The grouping has its genesis in an outburst from one of the Paulson & Co's partner at the Denver Gold Forum last year. In an onslaught that rattled the false teeth of some attendees the partner, Marcelo Kim, said the sector needed to address high executive pay, cozy board appointments and value-destroying mergers and acquisitions. Many attendees must have rushed home to see that Paulson was not on their register and called their financiers to make sure they were not included in any financings.

The trouble with this cabal, for majors, is that the constituents of the group make up exactly the type of people that Big Mining has milked over and over again for capital raises. If that worm turns then there are no more invertebrates of size out there to hoodwink any more.

Let's see if this movement gains any traction. Playing "happy families" with the executives of major miners one moment and biting that hand (that grabs the candy) the next is going to make for some nervous moments all round.



**Mining Model Portfolio as at the 1st of November 2018**

Security		Initiated	Currency	Price		Portfolio	Increase	Target
				Avg.	Current	Weighting	in Value	
<b>Long Equities</b>								
<b>Various Large/Mid-Cap</b>	Teck Resources (TECK.B)	5/29/2009	CAD	22.46	27.21	8.4%	21.1%	\$38.00
	Sherritt International (S.to)	7/11/2013	CAD	1.28	0.56	4.4%	-56.2%	\$2.50
	Metals X (MLX.ax)	29/5/2014	AUD	0.67	0.48	4.6%	-28.5%	\$1.00
<b>Trading House</b>	Noble Group (CGP.SG)	15/11/2017	SGD	0.20	0.08	1.3%	-59.8%	\$0.30
	Uranium	10/20/2010	CAD	5.36	4.54	8.0%	-15.4%	\$6.00
<b>Zinc/Lead Plays</b>	GoviEx (GXU.v)	6/29/2015	CAD	0.08	0.22	6.2%	167.7%	\$0.50
	Zinc ETF (Zinc.L)	6/2/2010	USD	7.63	7.55	7.9%	-1.0%	\$11.00
	NorZinc (NZC.to)	12/9/2011	CAD	0.82	0.09	0.3%	-89.0%	\$0.70
<b>Gold Producers</b>	Ascendant Resources	10/31/2016	CAD	0.49	1.00	6.6%	104.5%	\$1.70
	Telson Mining (TSN.V)	3/19/2018	CAD	0.79	0.41	3.3%	-48.1%	\$2.00
	Southern Silver Exploration	8/25/2016	CAD	0.49	0.19	1.1%	-60.8%	\$0.35
<b>Copper Producer</b>	Para Resources (PBR.v)	2/17/2017	CAD	0.23	0.17	2.0%	-26.1%	\$0.58
	Westgold (WGX.ax)	12/6/2016	AUD	2.01	1.11	2.3%	-44.8%	\$2.40
<b>Coking Coal</b>	Coro Mining (COP.to)	2/23/2015	CAD	0.03	0.05	1.2%	66.7%	\$0.30
<b>Beryllium</b>	Colonial Coal (CAD.v)	6/4/2018	CAD	0.35	0.29	2.7%	-17.1%	\$1.10
<b>Driller</b>	IBC Advanced Alloys (IB.v)	4/29/2016	CAD	0.30	0.28	0.7%	-6.7%	\$0.50
<b>Tungsten Producer</b>	Cabo Drilling (CBE.v)	9/28/2016	CAD	0.025	0.02	0.9%	-20.0%	\$0.08
<b>Copper Explorer</b>	Almonty Industries (All.v)	7/31/2015	CAD	0.36	0.77	9.1%	112.5%	\$1.00
<b>Lithium</b>	Asiamet Resources (ARS.v)	4/28/2016	CAD	0.05	0.06	2.0%	13.8%	\$0.12
	Phoenix Global Mining	9/28/2018	GBP	0.35	0.29	2.6%	-18.6%	\$0.74
	Panoro Minerals (PML.v)	1/22/2018	CAD	0.37	0.23	1.6%	-37.0%	\$0.65
	Western Copper & Gold	4/25/2017	CAD	1.57	0.82	1.9%	-47.8%	\$2.74
<b>Scandium Explorer</b>	Neometals (NMT.ax)	7/31/2014	AUD	0.30	0.26	5.5%	-14.2%	\$0.45
	Lithium Power Intl (LPI.ax)	10/25/2017	AUD	0.44	0.24	1.6%	-45.5%	\$1.38
<b>Gold Explorer</b>	Scandium International	8/23/2016	CAD	0.14	0.23	3.3%	64.3%	\$0.50
	Platina Resources (PGM.ax)	10/25/2018	AUD	0.07	0.06	2.7%	-7.7%	\$0.18
<b>Graphite Developer</b>	Banyan Gold (BYN.v)	11/14/2017	CAD	0.06	0.04	2.2%	-35.5%	\$0.15
<b>Rare Earths</b>	Talga Resources (TLG.ax)	8/25/2016	AUD	0.27	0.49	2.7%	84.9%	\$0.90
	Northern Minerals (NTU.ax)	6/9/2011	AUD	0.14	0.08	2.9%	-43.3%	\$0.28
	Neomaterials (NEO.to)	10/25/2018	CAD	17.32	17.8	6.3%	2.8%	\$23.00
<b>NET CASH</b>						<b>747,604</b>		
<b>Short Equities</b>								
<b>Shorts</b>	NioCorp (NIO.to)	9/28/2018	CAD	0.61	0.56	59.3%	8.20%	\$0.40
	Lithium Americas (LAC.to)	10/25/2017	CAD	10.10	4.50	19.9%	55.40%	\$5.00
	Galane Gold (GG.v)	4/28/2016	CAD	0.06	0.06	20.8%	0.00%	\$0.03

Current Cash Position	747,604
Current Liability on Shorts Not Covered	242,063
<b>Net Cash</b>	<b>989,667</b>
Current Value of Bonds	0
Current Value of Long Equities	3,232,182
<b>TOTAL VALUE OF PORTFOLIO</b>	<b>4,221,849</b>

## Important disclosures

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