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Alta Zinc faces burden of history, disclosure

Prior disappointments, a misguided market regulator and awkward strategic positioning are conspiring to hobble the investment performance of Alta Zinc.

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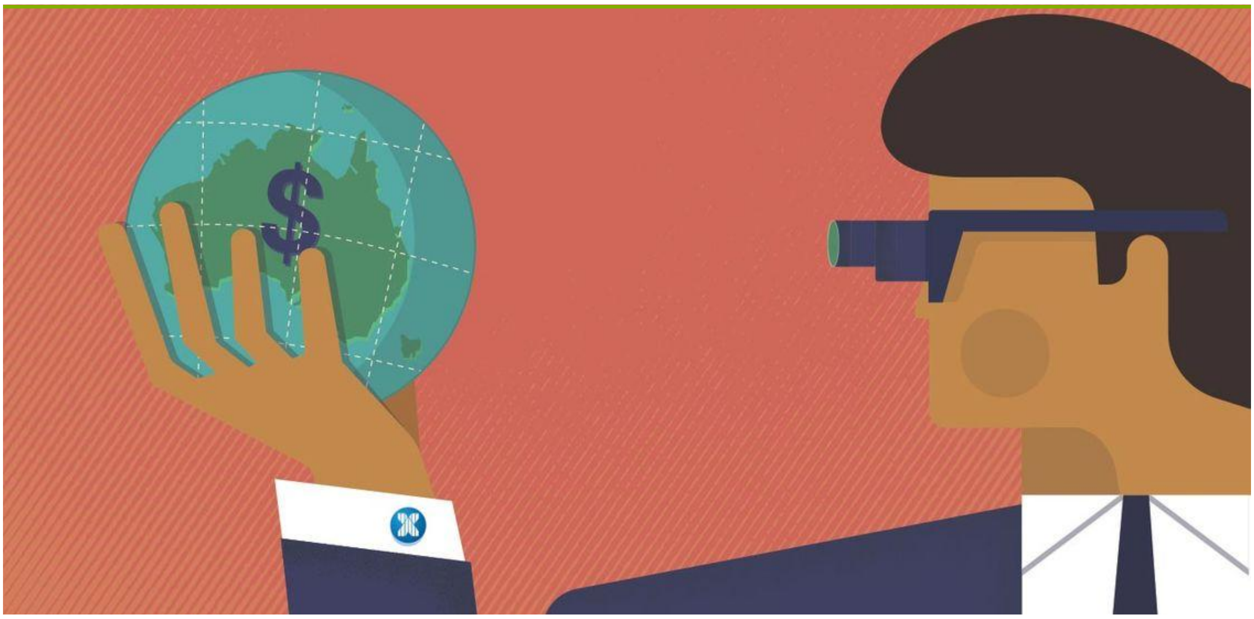

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The Gorno zinc mine, about 90km northeast of Milan and closed since 1985, seemed set for a new lease of life when Perth-based uranium explorer Energia Minerals purchased the mining concession in 2014.

Energia, now Alta Zinc, foresaw a speedy production start. The mine had been closed when owner ENI decided to concentrate on its energy business, not through any technical shortcomings. The state-owned company left behind 280km of underground workings, reaching mineralisation 400m below the surface. A potentially quick and cheap restart was beckoning.

Infrastructure, personnel and market access were straightforward. Smelters were within easy reach. The mine's zinc and lead concentrates had proven market appeal. The time frame for metallurgical test work was considerably shortened by having access to plentiful historical data. The zinc price was expected to rise.

Four years ago, investors were told they had only six months to wait for a definitive feasibility study. In anticipation, the company's market capitalisation climbed to A$46 million in early February 2017 before plummeting 78% through the first half of the year, after directors decided to reappraise their plans.

The downward share price trajectory continued until as recently as March this year. Since late 2016, the company has raised A$18 million from seven trips to the capital market and 2.1 billion new shares, lengthening the trail of disenchanted investors.

Alta is now stuck in an investment no-man's land. With a 3.3 million tonne resource, it is sufficiently far down the development path to have removed the likelihood of discovery surprise but not so far along that investors are prepared to give it credit for future cash flows.

A definitive feasibility study will not be finished before mid-2022 leaving investors with a long wait for something they will have been promised five years earlier.

A January 2019 project study proved counterproductive in recruiting new investors. Under the rules of the Australian market regulator, Alta could not proffer details about production targets as long as it had to rely on a 36% inferred component in its resource estimate. Prevented from publicly outlining production plans, the company could not discuss capital or operating costs.

During a webinar briefing earlier this month by chief executive Geraint Harris, his corporate adviser described the company as "seriously undervalued". Without being able to disclose basic information about the company's plans, neither could substantiate the assertion.

Regulatory constraints on what can be disclosed are designed to protect investors from industry charlatans tempted to exaggerate the size and potential value of their proposed developments. However well intentioned, such a regulatory approach can compromise market efficiency.

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Initial capital cost estimates for Gorno and an overall operating cost estimate consistent with standard industry practice for feasibility studies have been completed but kept under wraps at the behest of the market regulator.

Censoring details critical to judgements about valuation promotes an uneven playing field. Market regulators have effectively condoned insider trading. The bulk of Alta shareholders are being asked to decide how much they should pay without having material information about the company's project economics. Meanwhile, Alta directors are lining up to purchase shares in the company's latest offering with privileged access to the available information, thanks to the corporate regulator.

Comparable companies in other market sectors are regulated with a far lighter touch. The difference is most noticeable in the latitude afforded biotechnology stocks.

Companies engaged in drug development have similar risk characteristics as early stage miners. A junior pharmaceutical company about to embark on a phase 1 drug trial has a statistically low chance of jumping the various research and regulatory hurdles on the way to commercialisation.

Despite the risks to success, early stage drug companies typically discuss the size of the market opportunity and their assessments of the revenue potential in pitching for retail investor support.

Raising expectations about a drug's future income stream before safety and efficacy have been demonstrated is directly equivalent to a mining company talking about prospective production targets without a resource estimate.

By more heavily controlling what miners can say to attract retail investors, the market regulator tilts the investment balance in favour of the apparently more genteel pharmaceutical sector.

As well as its Gorno prospect, Alta has its eye on an early stage exploration property, also in northern Italy, prospective for cobalt-nickel mineralisation. In this way, too, Alta is following a well-worn industry path based erroneously on the belief that two uncertain projects create more value than one completed development.

If investors were offered a chance to buy an investment apartment, they would want to know the required outlay, the rental income and the potential capital appreciation. If the net result exceeded their borrowing costs, the deal would make sense.

If the same investors were then told that the rental income would be used to buy another currently unspecified asset at an unknown price and with an uncertain return, their enthusiasm would wane considerably. A higher return from the first project (that is, a lower purchase price) would be needed.

The same investment principles apply to mining stocks in public markets. Investors should always want to discount the value of an initial project knowing that any prospective cash flows will be deployed elsewhere.

Alta's inclination to already look for greener pastures undervalues the investment appeal of its primary project.

A planned 2,000m drilling program, scheduled for completion this year, will go some way to better defining the resource base and facilitating a clearer understanding of the investment proposition.

With more certainty about the resource size and quality, clearer judgements can be made about how much to pay.

Alta remains favourably positioned with tunnelling and a mine portal already in place. Unfortunately, the promise is not new. History is now the principal handicap to rejuvenating investment market appeal. The historical burden will not be easily shed, making Alta a high opportunity cost investment.

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